

The Government is committed to promoting fairness alongside flexibility and enterprise to ensure that everyone can take advantage of opportunities to fulfil their potential. The Government's reforms of the welfare state reflect its aims of eradicating child poverty, supporting families to balance their work and family lives, promoting saving and ensuring security for all in old age. The Government is also committed to a modern and fair tax system that ensures that everyone pays their fair share of tax. This Pre-Budget Report sets out the next steps the Government is taking to support these aims, including:

- **announcing that from April 2007, the value of the child element of Child Tax Credit will rise by £80 to £1,845 per year;**
- **from April 2009 additional support for all families, with every mother-to-be becoming eligible for Child Benefit from week 29 of their pregnancy, so that women will be up to £200 better off;**
- **an extension of the Warm Front programme, targeting 300,000 of the most vulnerable pensioner and other households, community by community;**
- **making Individual Savings Accounts (ISAs) permanent, beyond 2010, to provide stability for savers and certainty for the industry. In addition, the introduction of a package of reforms to the ISA, designed to simplify the regime, will make it more flexible for savers and providers and further promote saving;**
- **a package of measures responding to the consultation on the role of the third sector in social and economic regeneration, including the establishment of a new £30 million Community Asset Transfer fund and the guarantee of three years of funding passed on to third sector organisations;**
- **the establishment of an international research collaborative for the development sciences, led by a high level steering board including leading scientists; and**
- **further reforms to modernise the tax system and protect tax revenues, including work to tackle avoidance.**

5.1 The Government's aim is to promote a fair and inclusive society in which everyone shares in rising national prosperity and no one is held back from achieving their potential by disadvantage or lack of opportunity. The Government is committed to advancing fairness and flexibility together, so that all people, at all stages of life, can benefit from the UK's modern and dynamic economy.

SUPPORT FOR FAMILIES AND CHILDREN

5.2 The Government believes that every child, irrespective of background or circumstances, deserves the best start in life. To achieve this, since 1997, the Government's strategy has been to reform financial support for families with children, help parents into work and provide better public services for children and their families.

Eradicating child poverty

5.3 To ensure that every child gets the best start in life, the Government has set itself the goal of eradicating child poverty in a generation. This commitment has been underpinned by stretching targets to reduce by a quarter, and then by a half, the numbers of children living in relative low-income households.

Progress to date 5.4 In the 1980s and early 1990s, child poverty more than doubled. Since 1999, the Government has decisively reversed this upwards trend. Child poverty rates have fallen faster than in any other European country. Between 1998-99 and 2004-05, the numbers of children in relative low-income households fell from 3.1 million to 2.4 million, at the same time as average incomes grew by 2.4 per cent per year in real terms. Against a fixed income poverty line, 1.8 million children have been lifted out of poverty since 1996-97. And as the poorest families have seen their incomes rise, they have spent more on their children's needs,¹ and there are fewer families unable to afford key items such as new shoes and winter coats.²

5.5 The Government's first Public Service Agreement (PSA) target was to reduce the number of children in relative low-income households by a quarter between 1998-99 and 2004-05. Data released in March 2006 showed that this measure of poverty had fallen by 700,000, the equivalent of 23 per cent (before housing costs) or 17 per cent (after housing costs). These reductions represent a strong improvement and the Government remains committed to halving the numbers of children in poverty by 2010-11.

Halving child poverty 5.6 *The Child Poverty Review*³ set out the Government's strategy for halving and eradicating child poverty, and the Government will continue to take this forward. Lisa Harker has conducted an external review for the Department for Work and Pensions (DWP) on how it can maximise its contribution to halving child poverty,⁴ and her conclusions are currently being considered. This chapter also sets out steps to improve support for children and young people.

Financial support for families

5.7 Since 1997 the Government has radically reformed the way it provides support to families with children, recognising the benefits of a good start in life and that families with children face additional costs. This support is delivered through a combination of Child Tax Credit (CTC) and Child Benefit.

Increased support for families 5.8 Tax credits are the central component of the Government's programme of financial support for families and are reaching far more low- and moderate-income families than any previous system of income-related financial support, benefiting around six million families and ten million children. Figures published in March 2006 showed that in the first year of new tax credits (2003-04), 79 per cent of eligible families were claiming CTC, while the proportion of the money claimed was even higher, at 87 per cent. Some 89 per cent of low income working families claimed tax credits in 2003-04, a higher level of take-up than for Working Families' Tax Credit (WFTC) and significantly higher than for Family Credit. In their first year of operation, take-up was 65 and 57 per cent for WFTC and Family Credit respectively.

¹ *That's where the money goes*, Gregg, Waldfogel and Washbrook, 2005.

² *Families and children study*, Department for Work and Pensions (DWP), 2006.

³ *Child Poverty Review*, HM Treasury, July 2004.

⁴ *Delivering on child poverty: what would it take?* Lisa Harker, November 2006.

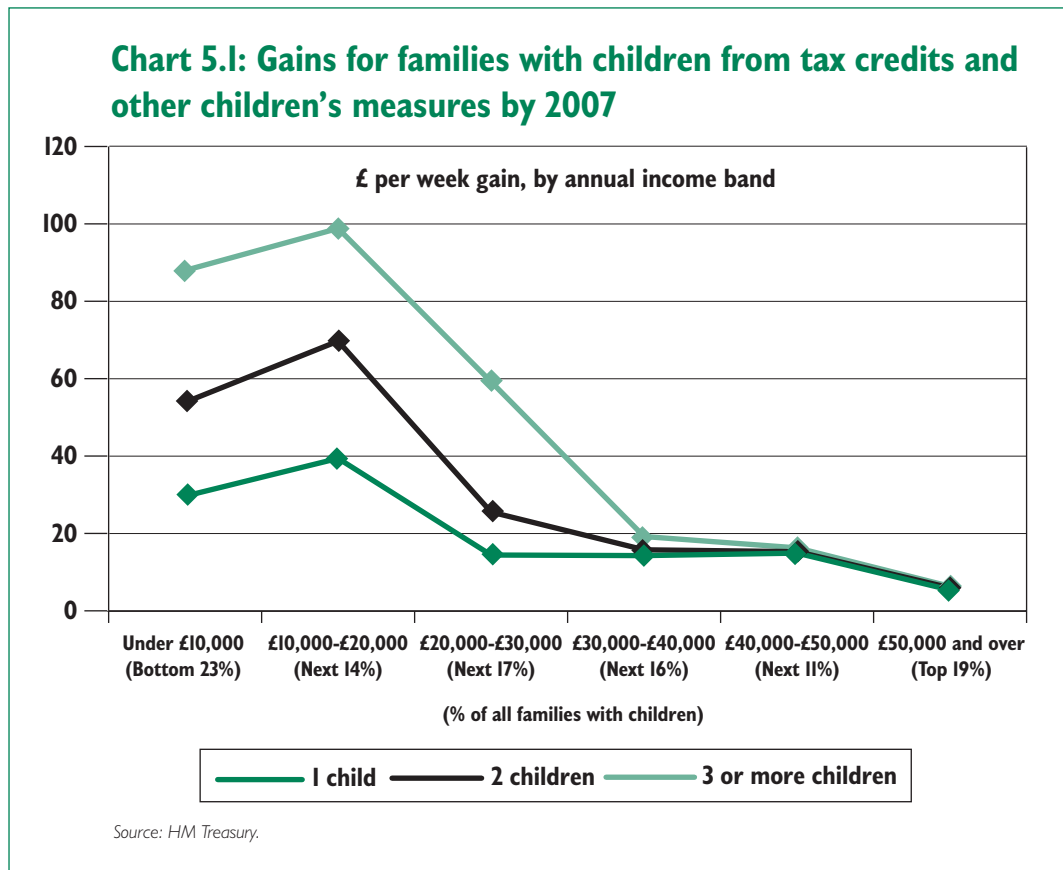
5.9 This Pre-Budget Report announces that, **from April 2007, the child element of CTC will increase by £80 to £1,845 a year**, in line with the Budget 2006 commitment to raise the child element at least in line with earnings until the end of this Parliament. This represents a total increase of £400 since its introduction in April 2003. In 2007-08, a family with two young children and a full-time earner on £16,500, half male mean earnings, will receive over £110 per week in CTC and Child Benefit, more than double the equivalent support in 1997-98. Table 5.1 shows the levels of support that CTC and Child Benefit will provide for families from April 2007.

Table 5.1: Minimum annual levels of support for families from April 2007

Annual family income	up to £14,495	up to £50,000	all families
Per cent of families	30	80	100
1 child	£3,330	£1,490	£940
2 children	£5,810	£2,120	£1,570
3 children	£8,280	£2,740	£2,200

Making families better off 5.10 Chart 5.1 shows the impact of the Government's measures to support families since 1997. It shows that all families have benefited but the greatest benefit has gone to families with low to middle incomes. For example, families with two children and an income in the range £10,000 to £20,000 are on average around £70 a week better off.

5.11 The Government recognises the importance of a healthy diet in the final weeks of pregnancy and the additional costs faced by parents when their children are born. Low-income families may already claim the Sure Start Maternity Grant, worth £500 per child, to help with these additional costs. **This Pre-Budget Report announces additional support for all families. From April 2009, every mother-to-be will become eligible for Child Benefit from week 29 of their pregnancy, so that women will be up to £200 better off by the birth of their first child and up to £130 better off at the birth of subsequent children.**



5.12 As a result of the Government's reforms to the personal tax and benefit system and the National Minimum Wage, by April 2007 and in real terms:

- families with children will be on average £1,550 a year better off, while those in the poorest fifth of the population will be on average £3,450 a year better off;
- a single-earner family on half male mean earnings with two children will be £3,900 a year better off; and
- a single-earner family on male mean earnings with two children will be £255 a year better off.

Tax credits 5.13 In the 2005 Pre-Budget Report, the Government announced a series of reforms to improve the tax credit system by increasing certainty for claimants. The Government has begun to introduce these changes, for example, by increasing the income disregard to £25,000 and shortening the renewal window to five months. End of year adjustments leading to an overpayment fell by a fifth between 2003-04 and 2004-05. Once the measures announced in the 2005 Pre-Budget Report come fully into effect, the level of end-year adjustments is expected to fall by a further third.

5.14 In addition to these policy measures, HM Revenue and Customs (HMRC) has worked hard to improve its service to claimants by improving its procedures, making its communications more claimant friendly and its forms easier to complete. This has meant fewer overpayments are caused by processing or software error and accuracy in processing and calculating awards rose to 97.7 per cent in 2005-06 – up from 78.6 per cent in 2003-04. This is a comparable level to HMRC's performance in handling claims for Child Benefit.

5.15 Following the successful reduction of the window to five months earlier this year, **the Government will shorten the renewal period to four months in 2007**. This will further reduce the time over which claimants are paid on potentially out of date information.

Box 5.1: Tax credits have improved choices for working families

The introduction of tax credits has improved choices for working families and eased the burden on parents seeking to balance work and family. By increasing financial support for families with children, tax credits make it easier for one parent in a couple to work part-time or remain at home to care for their children. Tax credits have also improved financial returns to work, helping parents to re-enter employment after a period of caring for their children.

This can be shown by considering the effects of the Government's reforms on a family with two children under the age of 11, with a single earner on half male mean earnings (£16,500). Where one parent chooses not to work, the family is now £4,500 a year better off than under the 1997-98 tax and benefit system, increasing the level of support should one parent choose to stay at home to care for the children full-time. Should the non-working partner return to work, the family would then find itself an additional £2,200 a year better off, compared to £1,200 a year in 1997-98. In this way the Government is supporting families' choices over balancing work and family life, by providing more support to stay at home and better incentives to return to work.

Child maintenance **5.16** The payment of child maintenance can make a significant difference to the lives of low-income families and lift many children out of poverty. Since 2003, parents with care on the new child support scheme have been able to keep the first £10 per week of any child maintenance paid without it affecting their benefit entitlement. This is known as the Child Maintenance Premium and currently over 50,000 parents are benefiting from it. By the end of 2008 the Government **will extend the Child Maintenance Premium to parents with care on the old child support scheme**. It is estimated that this will benefit an extra 40,000 parents with care, with an additional 15,000 more children receiving the full amount of maintenance paid by the non-resident parent. The Government's forthcoming child maintenance White Paper will set out further reforms to help tackle child poverty; promote parental responsibility; provide a cost-effective and efficient service and value for money for the taxpayer; and improve simplicity and transparency.

Financial support for young people

5.17 Skills are key to increasing individual opportunity, improving labour market flexibility and boosting productivity. The Government has an ambition to raise participation in education and training from 75 per cent to 90 per cent at age 17 by 2015, so that all young people have the skills they need to achieve in a modern, global economy. In support of this, the Government is committed to a vision of a single, coherent system of financial support for 16-19 year olds, which ensures that all young people have the support and incentives they need to participate and achieve in education and training. The Leitch Review of Skills, published on 5 December and described in Chapter 3, sets out new ambitions for the UK to reach world-class skills levels.

Engaging the most disadvantaged young people **5.18** Evidence suggests that where young people spend prolonged periods unemployed or inactive, it has a negative impact on their employment prospects and life chances. Since April 2006, the Government has been piloting Activity Agreements and Allowances targeted on the most disadvantaged 16-17 year olds. These extend conditional financial support to this group, setting a clear expectation that young people will progress into learning, and offering them the financial support and opportunity to do so. The findings of this pilot will inform the review of financial support for 16–19 year olds. This Pre-Budget Report **announces that the Government will consider extending these pilots to support young people to make the transition back into learning.**

Support for children and young people

Review of children and young people **5.19** Budget 2006 launched a joint HM Treasury and Department for Education and Skills (DfES) policy review to inform the 2007 Comprehensive Spending Review (CSR) on how to secure further improvement in outcomes for children and young people. Under the umbrella of this review, sub-reviews will focus on support for disabled children, youth services, and services for families caught in a cycle of low achievement. Further details are set out in Chapter 6.

Children in care **5.20** The state has a special responsibility for children in care, and yet outcomes for this group are extremely poor – both in absolute terms and relative to their peers. For this reason, these young people are at the heart of the Government's wider programme to tackle the poor outcomes and social exclusion of the most vulnerable groups in society. Fulfilling the commitment in the Schools White Paper⁵ to consult on a wide-ranging set of proposals to transform outcomes for children in care, the Government published *Care matters: Transforming the lives of children and young people in care*, for consultation in October 2006. A number of working groups have been established to consider particular issues, such as the long-term future of the care population, placement reform and best practice in schools. The Government will publish an initial response to the consultation, including a version for young people, in 2007.

Budget-holding lead professionals **5.21** *Support for parents: the best start for children*⁶ set out an ambition to promote greater personalisation of services. It announced a series of Single Account Holder pathfinders to test whether better service packages for children, young people and families can be delivered by giving lead professionals a budget with which to procure goods and commission services directly from providers. £10 million in additional funding over two years has been made available to support the pilots. Since June 2006, 15 pilots have been established in 16 local authorities and will run until April 2008.

⁵ *Higher Standards: Better Schools for All*, Department for Education and Skills, October 2005.

⁶ *Support for parents: the best start for children*, HM Treasury and Department for Education and Skills, December 2005.

Parent Support Advisers 5.22 *Support for parents* also announced £20 million to support the piloting of a new school-based outreach role, Parent Support Advisers, in over 600 primary and secondary schools in the most deprived areas. This new, preventative role is intended to support children and families where there are early signs that they could benefit from additional help. A total of 20 local areas have been selected to run the pilots and 100 schools now have Parent Support Advisers in place. It is anticipated that as many as 700 schools will have Parent Support Advisers provision by spring 2007.

Childcare and work-life balance

5.23 Flexible, affordable and high-quality childcare provision is an important element of the Government's strategy to both provide support to families and eradicate child poverty. *Choice for parents, the best start for children: a ten year strategy for childcare*, published alongside the 2004 Pre-Budget Report, set out the Government's long-term vision for childcare and early years services.

Delivering the ten year strategy 5.24 The Government is committed to ensuring that parents have greater choice and flexibility in balancing work and family life. From April 2007, paid maternity leave will be extended from six to nine months, and the Government has an aim of 12 months paid maternity leave by the end of the Parliament. The Government will also continue to examine the case for extending the right to request flexible working to parents of older children in the future.

5.25 Good progress has been made in delivering the other commitments set out in the ten year strategy, including:

- the creation of over 1,040 Sure Start Children's Centres, ahead of schedule, providing integrated early childhood services for children and their families (see Box 5.2 below);
- the creation of over 3,500 extended schools, offering additional services, out of school activities and greater engagement with parents and the local community, including high quality childcare between 8am and 6pm all year round;
- Royal Assent of the Childcare Act on 11 July 2006 that introduces new duties on local authorities to improve child outcomes and secure a sufficient supply of childcare and a new system of regulation and inspection for childcare and early education; and
- delivering high quality childcare, through new training opportunities and support from the Transformation Fund, and the creation of a new graduate Early Years Professional status, with the first graduates receiving training from September 2006.

Box 5.2: Sure Start Children's Centres

The Government is ahead of schedule on reaching a nationwide network of 3,500 Sure Start Children's Centres by 2010, which bring together early education, health, family support and employment support for young families. There are many examples across the country of children's centres transforming the lives of children and families. It will be vital for these centres to continue to develop innovative, locally based approaches to service delivery and to remain accountable to the communities they serve.

The Government also recognises the significant challenges involved in ensuring that excellent practice is spread across all centres so that they bring high quality services for all. To achieve this, DfES is taking a number of important steps, including:

- establishing a comprehensive performance management framework, including a set of key performance indicators, against which all centres will be accountable, and new statutory targets for local authorities introduced in the Childcare Act 2006;
- appointing a new consortium, Together for Children, which will oversee the roll out of all centres and ensure that good practice is spread effectively across the country; and
- developing tools to enable children's centres to benchmark their expenditure and services against others, and proposals to strengthen the ability of children's centre managers to monitor and improve value for money.

Affordability for families **5.26** The Government wants families to be able to afford flexible, high-quality childcare that is appropriate to their needs and continues to believe that the childcare element of the Working Tax Credit is the most effective way of delivering support for low- to moderate-income families. This offers parents support with up to 80 per cent of costs, up to a limit of £300 a week (£175 for one child). Alongside this, the £55 per week income tax and national insurance contributions (NICs) exemption for employer-supported childcare, is improving childcare affordability for parents.

Workplace nurseries **5.27** Budget 2006 announced £16 million of new funding to establish capital grants to help small and medium-sized employers' workplace nurseries. Investment will be delivered through Regional Development Agencies, led by the London Development Agency. Funds will be allocated in areas where there is most evidence of demand, particularly in areas of economic growth and regeneration. Grants for these areas will be announced early in 2007, based on proposals from small and medium-sized enterprises.

FAIRNESS FOR DISABLED PEOPLE

5.28 The Government is committed to improving the rights and outcomes of disabled people. The additional provisions of the Disability Discrimination Act 2005 came into force from December 2006. Most notably, all public sector organisations now have a statutory duty to promote equality of opportunity for disabled people, eliminate unlawful harassment and publish a Disability Equality Duty. Alongside the proposals set out in the Welfare Reform Green Paper⁷ including the reforms to incapacity benefits contained in the Welfare Reform Bill, currently before Parliament and detailed further in Chapter 4), this will enhance the opportunities for disabled people to participate fully in society by putting in place extensive support to help them re-engage with the labour market and gain employment, while also providing adequate support to those who are not able to work.

⁷ *A new deal for welfare: Empowering people to work*, Department for Work and Pensions, June 2006.

Improving the life chances of disabled people **5.29** The Office for Disability Issues (ODI), set up in December 2005, is taking forward the recommendations of the 2005 Strategy Unit report,⁸ in partnership with other Government departments. The ODI's first annual report was published in July 2006, and charts progress so far. The involvement of disabled people is critical in ensuring that policy design and service delivery respond to individual needs and aspirations. In order to ensure that the voices of disabled people are heard at the heart of Government, a new advisory non-departmental public body, Equality 2025: The United Kingdom Advisory Network on Disability Equality, will be launched in December 2006.

Independent living **5.30** The Government is committed to ensuring disabled people have choice and control over the support they need to live their everyday lives. Thirteen local authorities have been selected to run individual budget pilots, from spring 2006, which aim to improve the ability of disabled people and older people to live independently. These pilots are continuing to examine the effectiveness of giving individuals a choice of their budget in the form of cash, services or a combination of the two. As part of the 2007 CSR, the Government is looking at the effectiveness of the support that disabled people and children receive through the Children and Young People review, described earlier in this chapter, and the Mental Health and Employment review, described in Chapter 4.

PROMOTING SAVING, ASSET OWNERSHIP AND INCLUSION

5.31 The Government seeks to support saving and asset ownership for all across the lifecycle – from childhood, through working life and into retirement. Since 1997, the Government's savings strategy has focused on:

- improving the environment for saving – through a stable macroeconomy, a sound regulatory framework and employment opportunity for all;
- developing a range of savings opportunities suitable for each life stage – including the Child Trust Fund, Individual Savings Accounts and pensions;
- providing adequate incentives for saving through the tax and benefit system – for example, the Child Trust Fund, Individual Savings Accounts and the pensions tax regime all offer opportunities for tax-advantaged savings; and
- empowering individuals with the capability to make the right saving choices.

5.32 In aggregate, household wealth is higher than ever before. Net wealth, adjusting for rising personal debt, has grown by around 65 per cent in real terms since 1997.

Promoting saving and asset ownership for all

Child Trust Fund **5.33** The Child Trust Fund was introduced in April 2005 to promote saving and financial education and ensure that in future all children have a financial asset at age 18. Under the scheme, all newborn children receive £250 to be invested in a long-term savings and investment account, and children from lower-income families receive £500. Budget 2006 announced further payments into these accounts at age seven of £250 for all children, with children from lower-income families receiving £500.

⁸ *Improving the life chances of disabled people*, Prime Minister's Strategy Unit, January 2005.

5.34 Over 2.2 million Child Trust Fund accounts are now open. In the first year of operation, over three quarters of parents opened their child's account; over a third of children received an extra payment from the Government; and early evidence from providers suggests that there have been significant additional contributions into children's accounts.⁹ The Government will be doing more to promote engagement in the run-up to Christmas through a new advertising campaign, followed, in January, by a Child Trust Fund Week to raise awareness and participation among parents.

5.35 The Government recognises that children in care are a particularly vulnerable group, who often lack the support networks available to other children. In view of this, the Government announced in October 2006 that it **will provide an extra £100 per year for every child who spends the year in care**, in order that their Child Trust Fund provides a more significant asset for them to access on entering adult life.¹⁰

5.36 The Child Trust Fund will be used as a focus for financial education in schools, and will be a vital tool for engaging young children in developing the financial capability to manage their own Child Trust Fund at age 16 and to make well-informed decisions about their finances throughout their lives. Budget 2006 announced that the Government was exploring the use of a Schools Money Week as a focus for financial education. The Government is continuing to work with financial education bodies in developing the resources for teachers to support this initiative.

Individual Savings Accounts

5.37 Individual Savings Accounts (ISAs) were introduced in 1999 as a replacement for Tax-Exempt Special Savings Accounts (TESSAs) and Personal Equity Plans (PEPs). The objective has been to develop and extend the savings habit and to ensure that tax relief on savings is more fairly distributed. The evidence shows that ISAs have been successful in meeting these objectives: for example, over 16 million people – more than one in three adults – now have an ISA, with nearly £215 billion subscribed since their launch. ISA and PEP savings are supported by an estimated £1.8 billion a year in tax relief.

5.38 The Government is keen to build on this success. In order to provide stability for savers and certainty for the industry and following the conclusion of the review, the Government has announced that **it will make ISAs permanent beyond 2010, and that it will introduce a package of reforms designed to simplify the regime, make it more flexible for savers and providers and further promote saving**. These reforms are set out in Box 5.3.

Box 5.3: Individual Savings Accounts: proposed reforms

Following an internal review of the ISA regime, and in response to representations received, the Government proposed in November 2006 to:

- make ISAs permanent beyond 2010;
- guarantee an overall annual investment limit of at least £7,000;
- bring PEPs within the ISA wrapper;
- remove the Mini/Maxi distinction within ISAs;
- allow Child Trust Fund accounts to roll over into ISAs on maturity; and
- allow transfers from the cash into the stocks & shares component of ISAs.

The Government intends to implement this package of reforms as soon as practicable. Further detail on these reforms is published alongside this Pre-Budget Report, setting out proposals for implementation and seeking views on a range of practical issues.^a

^a *Individual Savings Accounts: proposed reforms* – available on the HM Treasury website at <http://www.hm-treasury.gov.uk>.

⁹ *Child Trust Fund: Statistical Report 2006*, HM Revenue & Customs, September 2006.

¹⁰ *Care Matters: Transforming the Lives of Children and Young People in Care*, Department for Education & Skills, October 2006.

Saving Gateway 5.39 Through the Saving Gateway, the Government is exploring the use of matching – a Government contribution for each pound saved. The aim is to encourage saving among lower-income households and to promote engagement with mainstream financial services. Evidence from an initial pilot, launched in 2002, confirmed that matching could encourage genuinely new savers and new saving.¹¹

5.40 A second pilot was launched in March 2005, involving around 22,000 participants. This is testing the effects of alternative match rates and contribution limits, initial endowments and the support of a range of financial education bodies. An interim evaluation report, published in July 2006, found that participants are overwhelmingly positive about the scheme and the matched payments they receive on their savings, and that participants intend to save regularly into their accounts.¹² The final evaluation of the second pilot is due to be published in spring 2007.

5.41 Many people use Christmas savings clubs and hamper schemes as a means of saving. In the light of recent events, the Government has asked Brian Pomeroy, Chair of the Financial Inclusion Taskforce, to conduct a review into these schemes. The aim of the review, which will report back by Budget 2007, is to both increase understanding of who uses the schemes and why, and also consider how the saving needs of this group of consumers might be better met by mainstream financial services providers. This review will not consider the regulatory aspects of the issue, which are being covered by the Office of Fair Trading and the Department of Trade and Industry, in consultation with the Financial Services Authority (FSA).

Promoting financial capability

5.42 Financial capability is vital to enable people to participate in a modern economy and to manage their finances effectively. People need access to information, the knowledge and skills to interpret it, and the confidence to take action.

5.43 The Government announced in the 2005 Pre-Budget Report that it would:

- address financial capability more explicitly in the curriculum by including it in the new functional mathematics component of GCSE mathematics and also in functional mathematics aimed at adults;
- encourage local authorities to provide more financial education to parents through Sure Start Children's Centres and locally-delivered family numeracy programmes; and
- provide information on opportunities for financial education to applicants for Social Fund Budgeting Loans.

5.44 On 18 October 2006, HM Treasury and the FSA hosted the first national conference on financial capability. The FSA has conducted a comprehensive survey into the financial capability in the UK and is delivering a number of projects to raise financial capability in schools and the workplace, and to target groups such as young people and prospective parents.¹³

5.45 The Government **will shortly publish a long-term strategy on financial capability.** This will be a consultative document, seeking views on how the Government can best use the levers at its disposal to reach people at key life stages and offer support for those most vulnerable to the consequences of poor financial skills. The strategy will also consider whether all consumers are being well served through current access to generic financial advice and how any gaps may be closed.

¹¹ *Incentives to save: Encouraging saving among low-income households*, University of Bristol, Personal Finance Research Centre, March 2005.

¹² *Interim Evaluation of Saving Gateway 2*, Institute for Fiscal Studies and Ipsos MORI Social Research Institute, July 2006.

¹³ *Financial Capability in the UK: Delivering Change*, Financial Services Authority, March 2006.

Promoting financial inclusion

5.46 Access to mainstream financial services can be restricted for many people on low incomes. *Promoting financial inclusion*¹⁴ outlined the Government's strategy, including the establishment of a Financial Inclusion Taskforce to oversee progress and a Financial Inclusion Fund of £120 million to support initiatives to tackle financial exclusion. In order to monitor these initiatives and identify areas where further work is required **the Financial Inclusion Taskforce will continue for an extra year to March 2008**. The Government will report on next steps for the financial inclusion strategy in the New Year.

Access to banking **5.47** Lack of access to banking services imposes costs on those who can least afford them. In December 2004, the banks and the Government agreed to work together towards a goal of halving the number of adults in households without a bank account and of making significant progress within two years. In its first annual report, the Taskforce concluded that steady progress had been made, but encouraged the banks to continue to address the difficulties faced in opening a bank account.¹⁵ The Taskforce will provide a full assessment of progress towards the shared goal in spring 2007. A working group, chaired by the Rt Hon John McFall MP, was established with the support of the Economic Secretary to the Treasury in July 2006, which is currently examining what mechanisms can be used to support the provision of free cash machines in low-income areas. The working group is expected to report back to the Economic Secretary before the end of the year.

Access to affordable credit **5.48** Many low-income households rely on credit products with interest rates of over 100 per cent. The Financial Inclusion Fund has been used to establish a 'growth fund' of £36 million to support third sector lenders in providing affordable and appropriate credit. Distribution of this fund commenced over the summer, and £34 million has now been committed. The Taskforce will monitor the impact of this funding in addressing financial exclusion. To protect investment in the growth fund, and to enhance the capacity and skills of staff and volunteers working for third sector lenders, the Government **will make funding available from the Financial Inclusion Fund to support the training requirements of third sector lenders**.

5.49 The Government also recognises the damage inflicted on individuals and neighbourhoods by illegal lending. The Government will make £1.2 million available from the Financial Inclusion Fund for pilots to tackle illegal lending and provide support to victims in accessing mainstream alternatives. Existing pilots covering Scotland and the West Midlands will continue for an extra year to 2008. The new funding will also be used to expand the operation of the scheme to Sheffield, West Yorkshire and Liverpool.

5.50 Following consultation, and in order to increase flexibility to lend to those on low incomes, the Government has increased the maximum rate that credit unions can charge on loans from 1 per cent a month to 2 per cent a month. The change came into effect on 1 June 2006. The Government has also consulted on extending community investment tax relief to the personal lending activities of community development finance institutions. The Government continues to consider the case for, and practicalities of, this extension. In order to reduce some of the increased risk and cost associated with lending to vulnerable groups, the Government will implement, later this month, a scheme where, under certain circumstances, third sector lenders can apply for repayment by deduction from benefits, where normal repayment arrangements have broken down.

¹⁴ *Promoting financial inclusion*, HM Treasury, December 2004.

¹⁵ *Financial Inclusion Taskforce: Report on progress towards the shared goal*, Financial Inclusion Taskforce, March 2006 – available on the Financial Inclusion Taskforce website at <http://www.financialinclusion-taskforce.org.uk>.

5.51 The Social Fund provides a safety net of grants and interest free loans for the most vulnerable in times of need. In April 2006, reforms to the Budgeting Loans scheme were successfully introduced that equate to an increase of funding of £210 million over the three years to 2008-09.

Access to money advice **5.52** Credit is a useful tool for managing expenditure for most people but some have difficulty managing their borrowing and become over-indebted. The Government recognises that face-to-face money advice is an effective mechanism for tackling problem debt and has committed £45 million from the Financial Inclusion Fund to achieve a step-change in supply. Funding commenced in April 2006, and more than 6,500 clients had been advised by the end of November. In total it is expected that there will be 350 new full-time equivalent advisers in place by the end of 2006. To build on the good progress made by these projects, the Government **will make an additional £2.5 million available, from the Financial Inclusion Fund, for the recruitment and training of more new advisers.** This funding will take the total number of new advisers to over 500. In addition, the Government has awarded £6 million to organisations across England and Wales to pilot debt advice outreach. Early evaluation has yielded positive results, suggesting that the outreach method can be an effective way of delivering money advice to harder-to-reach groups of financially excluded people.

Facilitating access **5.53** Following a recommendation from the Financial Inclusion Taskforce, the Government **will support, from the Financial Inclusion Fund, a £5.4 million campaign to assist financially excluded people to access mainstream banking and credit products.** The campaign, to be delivered through DWP, will work with trusted intermediaries in day-to-day contact with the financially excluded to achieve an increase in the awareness and take-up of mainstream financial services products across England, Wales and Scotland.

FAIRNESS FOR PENSIONERS

5.54 One of the most significant demographic trends projected to occur over the next ten years is the ageing of the population. For example, by 2017 the number of those aged over 85 will increase by over a third.¹⁶ To respond to the needs of today's older people and the challenges posed by demographic change, the Government has developed its Opportunity Age¹⁷ strategy, which promotes independence and well-being in later life and aims to ensure that the Government adapts to, and benefit from, an ageing society. A comprehensive programme of reforms seeks to ensure that pensioners can share in rising national prosperity, and that older people are able to play a full and active role in society.

5.55 The Government is committed to tackling pensioner poverty, rewarding saving, and helping extend working lives to enable people to meet their retirement income aspirations. Its strategy for pensioners is based on the principle of progressive universalism, providing support for all and more for those who need it most, through both financial support, access to services and action to tackle age discrimination, improve public services, and encourage and support healthy active ageing.

Fairness for today's pensioners

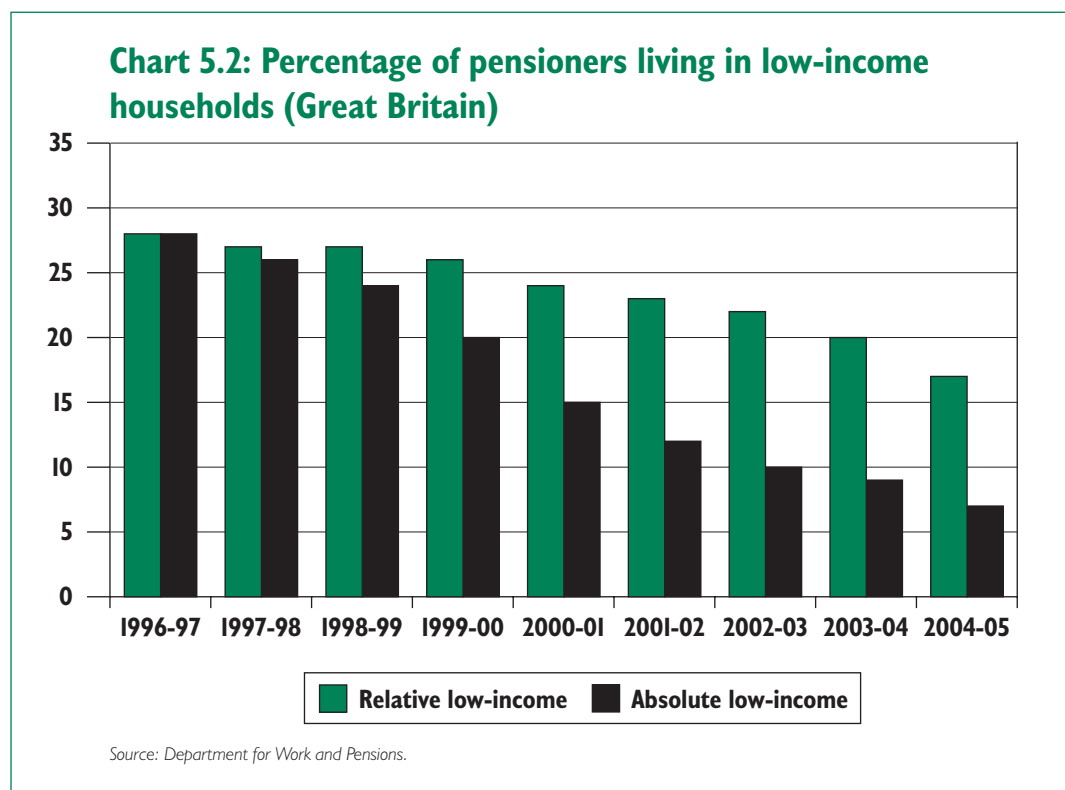
Security for the poorest pensioners **5.56** The Pension Credit, launched in 2003, is the foundation through which the Government provides security for the poorest. It is made up of the standard minimum guarantee (Guarantee Credit) that ensures a minimum income for those aged over 60, and the Savings Credit, which rewards those who have built up small savings for retirement. 2.7 million pensioner households currently receive Pension Credit: 2.1 million receive the Guarantee Credit, a take-up level achieved a year ahead of target and 1.9 million receive the Savings Credit.

¹⁶ *Long-term opportunities and challenges for the UK: analysis for the 2007 Comprehensive Spending Review*, HM Treasury, November 2006.

¹⁷ *Opportunity Age: Meeting the challenges of ageing in the 21st century*, Department for Work and Pensions, March 2005.

5.57 In 2004, the Government committed to uprating the guarantee element of the Pension Credit in line with earnings until 2008. Accordingly, from April 2007, it will rise to £119.05 for single pensioners and £181.70 for couples. From April 2007, the Savings Credit will also rise to a maximum of £19.05 a week for single pensioners and £25.26 for couples. As described later in this chapter, the Pensions White Paper¹⁸ announced that the guarantee element of Pension Credit will be uprated in line with earnings over the long term in order to ensure that the gains made against pensioner poverty are secure into the future.

5.58 Concentrating resources on the poorest pensioners has ensured that between 1996-97 and 2004-05 over one million pensioner households were lifted out of relative poverty and 2 million pensioner households were lifted out of absolute poverty. Half a million pensioner households have been lifted out of relative low-income poverty since the introduction of Pension Credit. As a result of the Government's reforms, the risk of a pensioner household being poor has fallen to 17 per cent and a pensioner is now no more likely to be poor than the population as a whole. Chart 5.2 below illustrates the progress that has been made in tackling pensioner poverty.



Support for all pensioners

5.59 The Government has continued to build on the foundations of support for retirement incomes provided by the basic and additional state pensions. The steps already taken to provide support for all pensioners include:

- guaranteeing that the April increase in the basic state pension will be in line with the Retail Prices Index for the previous September or 2.5 per cent, whichever is higher. From April 2007, the basic state pension will rise to £87.30. As described later in this chapter, the Government has also committed to uprating the basic state pension by earnings in the longer term;

¹⁸ *Security in retirement: towards a new pensions system*, Department for Work and Pensions, May 2006.

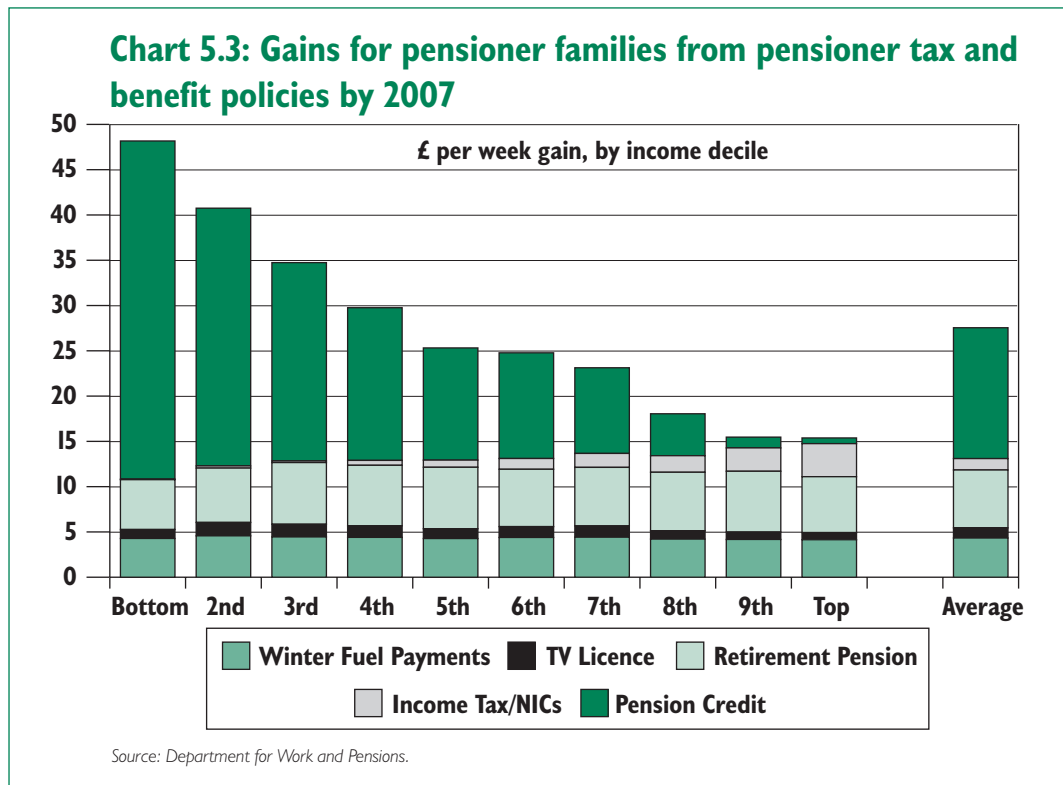
- the continuation of Winter Fuel Payments of £200 for households with someone aged 60 or over, rising to £300 for households with someone aged 80 or over, for the duration of this Parliament;
- free television licenses for those aged over 75, and free prescriptions and eye tests for those aged 60 and over;
- ensuring that those entering hospital receive their full entitlement to the basic state pension and some other benefits for the duration of their stay; and
- introducing free off-peak local area bus travel, and committing to extend this to off-peak nationwide bus travel from April 2008, for those aged over 60, and all disabled people, in England.

Helping vulnerable households heat their homes **5.60** The Warm Front programme aims to help low income households, including the poorest pensioners, heat their homes to an adequate standard of warmth by providing heating, energy efficiency measures, and benefit entitlement checks. Through the Energy Efficiency Commitment, energy suppliers also play an active role in helping keep the homes of the fuel poor warm, by offering a range of energy efficiency measures, like insulation, free of charge. They also offer discounted energy efficiency measures to all other households. Last year, the Chancellor announced a further £300 million to expand the Warm Front programme to enable pensioners on Pension Credit to have central heating systems installed free of charge and to provide £300 discounts for central heating systems for all pensioners without it. Efficient and effective coordination and delivery of these policies will be important if we are to achieve our fuel poverty goals. Evaluation of Warm Zone pilots earlier this year highlighted their potential role in facilitating this. To build on this work, the Government today **announces new investment of £7.5 million to improve the effectiveness of Warm Front and Energy Efficiency Commitment.** This will fund projects aimed at using an area-based approach to identify households and provide the right coordinated set of advice and measures to them.

Support for pensioners who pay tax **5.61** The Government is committed to supporting pensioners who pay income tax. Increases in the age-related tax allowances will mean that in 2007-08 no one aged 65 or over need pay tax on an income of up to £145 a week and around half of pensioners will pay no tax on their income.

Security for today's pensioners **5.62** The Financial Assistance Scheme was established in 2004 to assist those who lost significant amounts when their pension schemes were wound up. The Pensions White Paper announced that this scheme is being extended. Around 40,000 people, who were within fifteen years of their scheme pension age on or before 14 May 2004, will benefit at a total cost of £2.3 billion.

Effects of measures to support pensioners **5.63** As a result of measures implemented since 1997, the Government is spending around £11 billion a year more in real terms on pensioners, focusing support on those who need it most. As a result of the Government's tax and benefits measures, these households will be on average £2,100 a year, or around £40 a week, better off. Women pensioners have also particularly benefited from the Government's support for older people. 3.2 million women have gained an average of £31 a week, while 1.1 million men are £29 a week better off. Overall, pensioner households will be on average £1,450 a year, or around £28 a week better off. Chart 5.3 shows the distributional impact of the Government's measures to support pensioners.



Fairness for tomorrow's pensioners

5.64 Since 1997, the Government has been successful in delivering macroeconomic stability and high employment, providing an environment within which individuals can confidently plan for retirement, and where more people have the resources and opportunities to save. Going forward, the Government is committed to providing a clear and sustainable framework for retirement provision within which individuals can make informed choices about how much to save and when to retire.

Pensions Commission 5.65 The Government established an independent Pensions Commission in 2002 to review the adequacy of private pension saving in the UK, and advise on appropriate policy changes, including whether there is a need to “move beyond the voluntary approach”. The Pensions Commission found that although “on average, current pensioners are as well provided relative to average earnings as any previous generation”,¹⁹ there are a number of longer-term challenges to be addressed, including:

- rapid longevity gains leading to an increasing dependency ratio – an effect accentuated by the retirement of the “baby-boom” generation;
- inequalities in the state system, impacting especially on women and carers;
- reduced provision of pensions by employers; and
- failure of individuals to fill the gap left by employers, because substantial portions of the market are unserved by the pensions industry and there are behavioural barriers which impede rational long-term savings decisions.

¹⁹ A New Pension Settlement for the Twenty-First Century, Pensions Commission, November 2005, page 31.

Pensions White Paper 5.66 In May 2006, the Government responded to the Pension Commission's report in the White Paper, *Security in retirement: towards a new pensions system*. It proposed a series of changes to both the state and private pensions systems and announced that, "During the next Parliament, we will re-link the uprating of the basic state pension to average earnings. Our objective, subject to affordability and the fiscal position, is to do this in 2012, but in any event by the end of the Parliament at the latest. We will make a statement on the precise date at the beginning of the next Parliament." Together with the other proposals, this will create a platform for private saving, ensuring that anyone who has been in employment or caring throughout their working life could receive £135 a week in state pension at retirement – which is £20 a week above the guaranteed income level.²⁰

Fairness 5.67 To make the state pension fairer and more widely available, the Government proposes to reduce the number of qualifying years needed for a full basic state pension to 30 for those reaching state pension age from April 2010 and improve coverage for those caring for children and the severely disabled. As a result of the reforms, by 2025, over 90 per cent of women and men reaching state pension age will be entitled to the full basic state pension – compared to around 80 per cent without reform.

5.68 The White Paper also announced the intention to uprate the guarantee element of Pension Credit in line with earnings over the long term. Changes to the Savings Credit from 2008 will also ensure that it continues to focus resources on those with small savings. These changes will provide more certainty over the future role for Pension Credit, locking in reductions in poverty over time and ensuring that there are clearer incentives to save within the reformed system.

Simplicity 5.69 To simplify the current system, it is intended to reform the state second pension so that, by around 2030, it becomes a simple, flat-rate weekly top-up to the basic state pension. Under the new benefit, each qualifying year of work, parenting or caring will effectively top up the state pension by at least £1.40 a week at retirement.²¹ Additionally, the abolition of contracting out for defined contribution schemes, intended to occur at the same time as the uprating of the basic state pension is re-linked to average earnings, will remove another source of complexity in the current system.

Personal responsibility 5.70 Together, these state reforms provide a clear foundation for a new approach to private pension saving, the key element of which is the creation, in 2012, of a new scheme of portable, low-cost personal accounts. They are being designed and introduced primarily for individuals for whom suitable savings vehicles have not previously been available or affordable, particularly low to moderate earners. Personal accounts will help achieve the goal set out in the 2002 Green Paper, to "encourage simple and flexible savings products, broadening access to the financial services industry".²² They will entail:

- a minimum overall contribution of 8 per cent for the personal accounts of employees on earnings between around £5,000 and £33,000 a year – 4 per cent from the individual, 3 per cent from the employer and a further 1 per cent in the form of normal tax relief;²³
- automatic enrolment for employees into either the new personal accounts scheme or their own employer's occupational scheme providing it meets a minimum standard; and
- non-employees, including the self-employed and non-workers, will be able to opt into the scheme.

²⁰ Figure relative to average earnings. If expressed in 2005-06 prices, following these reforms, an average earner retiring in the 2050s will receive £340 per week in state pensions.

²¹ Figure relative to average earnings.

²² *Simplicity, security and choice: Working and saving for retirement*, DWP, December 2002, page 1.

²³ 1 per cent represents basic rate tax relief on individuals' contributions- in addition individuals may be entitled to higher rate tax relief.

5.71 Projections published by DWP estimate that 8 million people could be saving in a personal account. By retirement, their pension funds could be worth up to around 25 per cent more than if they were saving in the current system because of lower charges.

Sustainability 5.72 Following extensive consultation since the May White Paper, the Government intends to bring the proposed state pension reforms into effect through the Pensions Bill that was introduced in Parliament on 28 November. The proposed approach to the implementation and operation of personal accounts will be set out in a forthcoming White Paper later this month. Proposals will focus on the need to minimise the impact of personal accounts on those already providing good occupational pensions schemes and the burdens on employers, particularly small businesses. In addition, proposals will ensure that appropriate information is provided to enable people to make decisions on an informed basis. These proposals will build on the Government's current Informed Choice programme, plans for development of which will be set out in the forthcoming Financial Capability strategy.

Security for tomorrow's pensioners 5.73 These reforms build on earlier measures implemented by the Government to provide simplicity, security and choice in the pension system. The Government set up the Pension Protection Fund which, since its inception in April 2005, has offered protection to members of defined benefit occupational pension schemes in the event that the sponsoring company becomes insolvent when the pension scheme is in deficit. At the same time the Government set up the Pensions Regulator, which is a new risk based regulator overseeing a scheme specific funding regime to protect the benefits of members of work-based pension schemes.

Pensions simplification 5.74 Successive governments have offered tax relief on contributions to, and investment growth in, tax privileged pension schemes in order that those savings are used to produce an income in retirement. By saving in any tax-privileged pension vehicle, individuals are committing to using the resulting fund for the purpose of providing an income in retirement. This principle remains central to the simplified pensions tax regime introduced from April 2006. In order to ensure that the pensions tax rules continue to meet the original intention of the new regime, in addition to the announcements on Alternatively Secured Pensions (ASPs) and Pensions Term Assurance, the Government today **announces a package of measures that deliver technical improvements to the tax rules while consulting on areas for potential further deregulation with the industry**. Published alongside this Pre-Budget report, *The Annuities Market*, clearly sets out the Government's position regarding ASPs and changes now being made to their treatment through the pensions tax system.

Alternatively Secured Pensions 5.75 Annuities are the best way to secure a guaranteed income for life in retirement – a view endorsed by the Pensions Commission. ASPs were introduced to meet the specific need of certain groups that have a principled religious objection to the pooling of mortality risk in annuities. It was never the intention that ASPs would become a mechanism to avoid compulsory annuitisation, or to leave a tax-favoured lump sum that could then be passed on.

5.76 The Government therefore announces the **introduction of changes to the tax regime for ASPs at Finance Bill 2007 with effect from 6 April 2007**. There will be a requirement to withdraw a minimum level of income each year from an ASP fund and the facility to transfer funds on death as a lump sum to pension funds of other members in the scheme will be removed from the authorised payment rules, with these payments attracting an unauthorised payments charge. These proposals will bring practice and policy intention into line and provide a fair balance between meeting the needs of those with principled religious objections to annuitisation and the needs of the wider public. However, if these proposals prove unworkable, or there is continued evidence of the use of pensions tax relief to provide capital sums throughout retirement, the Government will consider whether to remove access to ASPs altogether. Draft legislation has been published today.

Pensions Term Assurance 5.77 The Government has become aware that, as a result of the flexibilities that the new pensions tax regime has brought in, life insurance policies that provide lump sum death benefits alone are being offered as personal pension arrangements eligible for pensions tax relief. This undermines the principles set out above. The Government will therefore work with the pensions industry to explore in time for the Budget, how the principles can be applied to pensions term assurance contracts. Any changes the Government decides to make will not effect either personal arrangements entered into before 6 December 2006 or existing types of employer arrangements.

SUPPORTING CHARITIES AND THE THIRD SECTOR

5.78 The third sector, including charities, voluntary and community organisations, cooperatives, mutuals and social enterprises, is integral to forming a fair and enterprising society, with a culture of volunteering and giving. The Government continues to provide a wide range of tax reliefs and other provisions to ensure that the third sector plays a key role in society.

Third sector review 5.79 Budget 2006 announced the largest ever consultation with the sector to inform a review into the future role of the third sector in social and economic regeneration. This consultation has reached in excess of 1,000 third sector organisations in nine regional events together with 84 sub-regional and sub-sectoral events. This joint HM Treasury and Cabinet Office review is overseen by a cross-departmental ministerial group.

5.80 *The future role of the third sector in social and economic regeneration: interim report*, published alongside this Pre-Budget Report, sets out the key messages highlighted by the consultation and areas where the Government is considering action. Such areas include the role of the third sector in creating stronger and more connected communities and giving voice to diverse groups; how the Government can foster a culture of volunteering and mentoring; and what more needs to be done to improve and implement best practice in relations between the third sector and all levels of Government. In addition, this Pre-Budget Report announces:

- **a new Community Assets fund of £30 million**, taking forward the Government's commitment as set out in the Local Government White Paper to make it easier for communities and community groups to take on the management or ownership of local authority assets;
- an expectation that when Government departments and their agencies receive their 2008-09 to 2010-11 budgets through the 2007 CSR, the flexibility and certainty of that three year funding will be passed on to third sector organisations that they fund as the norm rather than the exception; and
- for 2007-08, the Department for Communities and Local Government will allocate an extra £6.5 million in the Safer and Stronger Communities block of Local Area Agreements.

5.81 The final conclusion and recommendations of the review and a shared vision for the third sector will feed into the 2007 CSR. Further details of the 2007 CSR are set out in Chapter 6.

- Invest to Save Budget “Inclusive Communities”** **5.82** Budget 2006 announced a ninth Invest to Save Budget (ISB) allocation round which will conclude early next year. A further £13.5 million will be allocated to service delivery projects that promote partnerships between third sector organisations and local authorities to deliver more effective services to local people, in line with local needs and priorities. Successful projects will be announced at Budget 2007.
- 5.83** ISB has been running for over eight years and the projects within the ISB portfolio are delivering positive results. This Pre-Budget Report **announces a review of the fund** that will examine how successfully the ISB has delivered against its criteria of partnership working enabling innovation and long-term efficiency in public service delivery, and to what extent pilot projects have been rolled out more widely. The evidence gathered as part of the ISB review will be published in spring 2007.
- Volunteering** **5.84** Budget 2005 announced up to £100 million of funding for v, a new charity launched in May 2006 to take forward the vision of the Russell Commission²⁴ report by creating a new framework to support youth volunteering. In its first six months, v has already commissioned 67,000 new youth volunteering opportunities and has raised £15 million from 39 corporate supporters. **To build on this, the Government will be consulting on how a new generation of young people can do more to volunteer in the run up to the London 2012 Olympics.** The Government will also consider the case for further incentives to encourage volunteering.
- Social enterprise** **5.85** In November 2006, the Government published an action plan detailing measures to support and promote a dynamic and sustainable social enterprise sector. The action plan also set out proposals to ensure the availability of appropriate information, advice and finance to social enterprise, including making up to £10 million available to support existing Government investments to ensure that social enterprises also benefit.
- Charitable giving** **5.86** A number of sector representatives provided views on charitable giving as part of their response to the third sector review, which the Government is now considering. The Government is continuing to ensure that charitable giving is well supported with a range of tax reliefs and is keen to work with the sector in finding ways to raise awareness and uptake of the existing incentives for giving. HM Treasury and HMRC are therefore working with the Charity Commission and different parts of the sector to identify and minimise any administrative burdens that may inhibit the take up of charitable reliefs.
- Unclaimed assets** **5.87** The Government welcomes the banking industry’s commitment and progress towards introducing a scheme to allow genuinely unclaimed assets to be reinvested in the community with a focus on programmes for young people, financial education and financial exclusion. The industry and Government remain committed to reuniting owners with their assets as a first priority, and that a comprehensive reuniting exercise will precede any scheme launch. Once the scheme is in operation, owners will retain the right to get their money back.
- 5.88** In the Budget, the Government committed to consider the legal and accounting issues surrounding unclaimed assets. Having done this, the Government believes that in order to enable the banking industry to set up an unclaimed assets scheme, where the interests and rights of both consumer and industry are protected, it is necessary to bring forward enabling legislation. The Government will therefore bring forward proposals and consult widely.

²⁴ A National Framework for Youth Action and Engagement., Russell Commission, March 2005.

DELIVERING A MODERN AND FAIR TAX SYSTEM

5.89 A fair and modern tax system encourages work and saving, responds to business developments and globalisation and supports the provision of world-class public services. To ensure this, the Government will continue to develop a fair and effective tax system that provides a level playing field for all taxpayers.

Modernising tax administration

5.90 The majority of businesses recognise the role played by public services and public investment in promoting opportunities for investment and want to comply with their tax obligations. HM Revenue and Customs (HMRC) continues to work on transforming its relationship with business, and is consulting widely to drive that programme forward. Chapter 3 reports considerable progress over the past eighteen months, including how they are delivering the targets set at Budget 2006 to reduce the administrative burden on business of dealing with forms and returns, and audits and inspections. It also looks ahead at HMRC's long term vision for the relationship with business, setting out a comprehensive programme to transform the experience of dealing with HMRC and help businesses fulfil their tax obligations in the most efficient way.

Review of HMRC Links with Large Business **5.91** At Budget 2006, the Chancellor asked Sir David Varney, in his capacity as chairman of HMRC, to work with business representatives to identify how the needs of large business can be better taken into account in the administration of the tax system. The results of this work are set out in *Review of Links with Large Business*, published in November 2006. Implementation of the review's proposals will foster a relationship between business and HMRC built on greater trust and transparency, delivered by a risk-based audit approach which will ensure HMRC resources are focused on key risks so that issues are resolved quickly and companies obtain greater and earlier certainty about the tax implications of their commercial decisions. Further details are provided in Chapter 3.

Review of HMRC powers, deterrents and safeguards **5.92** As part of its ambition to create a world-class revenue department, the Government launched a review of HMRC powers and taxpayer safeguards in March 2005 to provide modern tools for the newly integrated HMRC. The review, informed by a consultative committee of tax experts, business representatives and others, is making good progress. In March this year HMRC launched its second consultation on the general principles of reform and in August more detailed consultation on modernising criminal investigation powers. HMRC is today publishing a summary of responses to the March consultation, which were generally supportive of the broad approach proposed. A detailed consultation on penalties for incorrect returns and a further consultation on criminal powers will follow shortly.

Reviewing HMRC administrative rules **5.93** In addition to minimising administrative burdens imposed on business through the tax system, as described in Chapter 3, HMRC is also reviewing its administrative rules. A new management act will deliver a modern, simpler and more consistent legislative framework for the administration of taxes that is easier both for taxpayers to understand and comply with, and for HMRC to operate. The first set of draft legislation for consultation covering the rules for notification and registration, returns, and assessments for income tax self assessment, corporation tax self assessment and VAT was published on 28 November and is available on the HMRC website. The aim, subject to the outcome of the consultation, is to introduce a Bill in the 2007-08 Parliamentary session.

HMRC online services **5.94** To increase the take-up of its online services, HMRC is investing in its supporting infrastructure and continuing to work with customers and other stakeholders on the implementation of Lord Carter's recommendations.²⁵ Legislation will be brought forward during 2007 to implement the changes which start in 2008. In July 2006, the Government accepted Lord Carter's revised recommendation for income tax self assessment, so that **the deadlines for filing returns for 2007-08 will be 31 October 2008 for paper and 31 January 2009 for filing online.**

Company filing dates **5.95** Following Lord Carter's recommendations and consultation by HMRC and Companies House, the Government will work to provide a single online filing facility by 2010. **To encourage earlier filing and give businesses certainty sooner, from 2008 the period during which an enquiry can be opened into a corporation tax return will be tied, for most companies, to the actual date HMRC receives the return rather than a fixed filing date.** HMRC will review the impact of these changes.

Modernising the tax system

5.96 The Government believes that the tax system should support its wider economic and social objectives by encouraging work and saving. The Government today announces measures to modernise the tax system and ensure that it keeps pace with developments in the business and personal sectors.

Tax-motivated incorporation **5.97** The Government is committed to ensuring that the small business tax system adapts to the changing business environment and that the UK is the best place in the world to start and grow a business. However, it remains concerned about the tax-motivated incorporation of the self-employed, which involves businesses taking advantage of structural differences in the tax and national insurance contributions (NICs) treatment that applies to companies. The Government will therefore continue to review how the system could be modernised, made simpler, more efficient and more competitive.

Tackling Managed Service Companies **5.98** At Budget 2006 the Government announced that it would respond to evidence of significant growth in Managed Service Company (MSC) schemes which are used to avoid paying employed levels of tax and NICs. There are existing rules – the Intermediaries legislation²⁶ – to ensure that the correct tax and NICs treatment is applied, but these rules are, in many cases, not being followed by MSCs. This gives them an unfair competitive advantage over compliant businesses and workers. In addition some workers are entering MSC schemes without understanding that they may be giving up employment rights.

5.99 The Government is **today announcing action to tackle Managed Service Company schemes** and is publishing a document on the measures and consulting on draft legislation to implement them. Personal Service Companies will not be within the scope of these measures with the Intermediaries legislation remaining in place as at present.

Income tax and NICs **5.100** The income tax personal allowances will increase in line with inflation in 2007-08. The NICs thresholds and limits will also increase in line with inflation. There will be no change to NICs rates for employers and employees, or to the profit-related NICs paid by the self-employed. Annex B provides further details of the rates and allowances in the tax and benefit system.

²⁵ *Review of HMRC online services*, Lord Carter of Coles, March 2006.

²⁶ Chapter 8, Part 2, Income Tax (Earnings and Pensions) Act, 2003; Section 4A, Social Security Contributions and Benefits Act 1992; Social Security (Intermediaries) Regulations 2000, SI 2000/727.

- Construction Industry Scheme** **5.101** The new Construction Industry Scheme will be introduced on 6 April 2007. The legislation to bring this into effect is being laid in Parliament this afternoon. It will reduce regulatory burdens and help the construction industry comply with its tax obligations. An increasing proportion of sub-contractors in the current scheme do not have their full tax and national insurance liabilities met by their deductions. To reduce the additional payments due after the end of the year, **the new scheme will have a standard deduction rate of 20 per cent.** To enable unregistered sub-contractors to start work sooner and encourage them to register, **the higher deduction rate will be 30 per cent.**
- Taxation of foreign profits** **5.102** The Government is determined to maintain the overall competitiveness of the UK, and since Budget 2006, has held productive dialogue with stakeholders on the taxation of foreign profits. Following the recent European Court of Justice (ECJ) judgment in Cadbury Schweppes, **changes to the Controlled Foreign Companies (CFC) rules are necessary to ensure they remain effective and to provide increased certainty for business.** The Government will consult with business in 2007 on a wider package of reform.
- 5.103** The Government will continue to defend the tax system robustly against legal challenges under EU law.
- Six year limitation period for all direct tax claims** **5.104** The Government **announces today that it will legislate to ensure that the limitation period for the recovery of direct tax paid by mistake of law is six years from the date of payment.** This is to ensure consistency with the limitation period for making claims in respect of direct taxes paid under assessment as a result of a mistake in a tax return, as specified in section 33 Taxes Management Act 1970 and paragraph 51 schedule 18 Finance Act 1998. This follows a recent House of Lords decision and restores the balance of interests secured by such a limitation.
- 5.105** Taking no action would risk unwarranted transfers from taxpayers in general to the current shareholders of certain claimant companies. The provision will have retrospective effect, but will not disturb the entitlement of those who have secured what amounts to a final judgment in their favour prior to 6 December 2006.
- Capital allowances for cars** **5.106** At Budget 2006 the Government published an analysis of the administrative burdens of the tax system, including capital allowances. The Government continues to examine opportunities for simplification and the recent consultation on modernising capital allowances for cars indicated businesses would welcome such reform. While there are significant opportunities to reduce administrative burdens, maximising the deregulatory gains of the reform depends on the design of incentives to purchase cleaner cars. The Government will therefore continue discussions with business, and present more detailed proposals at Budget 2007.
- Film tax relief** **5.107** The European Commission has now given final state aid clearance for the cultural test, which acts as the gateway to the new film tax relief. To ensure continuity in film tax relief during the transition to the new system, the Government has announced it will **extend section 42 relief for films until 31 December 2006. The new film tax relief will commence from 1 January 2007.**
- North Sea oil** **5.108** In the 2005 Pre-Budget Report, the Government announced that it would hold discussions with the North Sea oil industry on wider structural issues that have implications for the stability of the North Sea oil tax regime. These discussions were completed in September 2006 and the Government welcomes the constructive contributions from industry. The Government is considering the conclusions from these discussions and examining the options for further action on these strategic issues.

5.109 To address an anomaly identified during the course of these discussions, the Government today announces **the removal of fields from the charge to Petroleum Revenue Tax if they are redeveloped following full decommissioning.**

5.110 The Government also **announces the creation of a joint Government and industry working group** to examine the fiscal implications on the current regime in relation to the changed and dual use of North Sea infrastructure in, for example, carbon capture and storage.

Islamic finance 5.111 Since 2003 the Government has taken steps to level the tax and regulatory playing field for alternative finance products, including those designed to be Shari'a compliant. Building on this work, the **Government is working with stakeholders to develop legislative solutions that give equal tax treatment to alternative forms of bond, such as sukuk and amend the existing Community Investment Tax Relief scheme to cover alternative finance products.**

Life assurance companies 5.112 In 2006, the Government published a consultation on certain aspects of the taxation of life assurance companies. The Government welcomes the dialogue that it has had with industry and as an initial response **will bring forward legislation to amalgamate five business categories into one, simplify the rules applying on a transfer of insurance business and modernise the Crown option.**

Modernisation of Lloyd's insurance market 5.113 Following the meeting of the Chancellor's High Level Group on 18 October, a review is underway to look at modernising Lloyd's market practice. To support this process, the Government will introduce legislation to **address an anomaly in the tax framework for corporate members of the Lloyd's insurance market.**

General insurance reserves 5.114 To simplify the tax treatment of general insurance reserves the Government **will introduce legislation to repeal the current complex taxation rules and replace them with a narrowly targeted revenue protection measure.** Consultation will continue to finalise the scope of the legislative changes.

International accounting standards 5.115 Following consultation with business, new tax rules will be introduced for securitisation companies. The tax rules for financial instruments will be modified to address issues arising from the adoption of international accounting standards. Pending the outcome of further discussions, the corporation tax treatment of unclaimed bank balances will be deferred.

Sale and repurchase agreements 5.116 The Government will **consult with business with the aim of simplifying the tax legislation dealing with sale and repurchase agreements** for companies in order to improve the operation of the legislation and reduce compliance costs for companies. Draft clauses will be published shortly.

Stamp duty & stamp duty reserve tax 5.117 The Government will **exempt from stamp duty reserve tax (SDRT), with effect from 1 February 2007, purchases of shares in non-UK resident exchange traded funds** to support development and innovation in the market. It is also discussing with business what measures may be necessary to ensure that reliefs for Stamp Duty on Shares and SDRT continue to operate effectively following the implementation of the EU Markets in Financial Instruments Directive (MiFID) in November 2007.

Changes to the offshore funds tax regime 5.118 The Government will consult with industry to ensure tax rules in the Offshore Funds Regime do not act as a barrier to commercial development of multi-tiered funds. While consultation proceeds, the Government **will legislate in Finance Bill 2007 to address an immediate issue affecting existing multi-tiered fund structures.**

- Authorised Investment Funds owning property** **5.119** Alongside the introduction of UK-REITs, the Government has been considering the taxation of Authorised Investment Funds that invest in property. The Government has been consulting with interested parties and has identified a number of significant challenges. The Government will continue dialogue with stakeholders to establish how best to address these challenges.
- EU Review of VAT and Financial Services** **5.120** In the 2005 Pre-Budget Report, the Government announced it would delay implementation of the March 2005 ECJ judgment in the case of Arthur Andersen & Co Accountants concerning VAT and insurance-related services, pending progress in the European Commission review of the VAT treatment of financial services and insurance. The Government will continue to monitor the progress of the review in deciding whether to make the necessary changes to UK law, and will provide industry with sufficient notice following any decision to implement.
- VAT: special method of declaration** **5.121** Following informal consultation with affected businesses, the Government **will introduce from 1 April 2007 changes to the VAT rules that allow partly-exempt businesses to use bespoke calculation methods to agree how much VAT they can recover.** For the vast majority of the 20,000 businesses affected, these changes will simplify and speed up the administrative process for agreeing special methods of declaration. These changes will also require businesses to confirm that their proposed method gives a fair tax result. The new rules will also allow businesses to include the VAT on certain overseas supplies within their calculation method, which they currently have to reclaim separately.
- VAT: retention of records** **5.122** Following consultation with businesses, the Government **will bring forward changes in Finance Bill 2007 to clarify the VAT rules on which business records should be retained by the seller or passed to the buyer when a business is sold as a going concern.** This simplification measure will help businesses to retain or acquire the records necessary to ensure compliance with their tax obligations without imposing additional complexity or cost.
- Alcohol duty** **5.123** The Government is working with the alcohol industry to develop a shared vision of the alcohol duty regime that better reflects modern trade practices. Over 40 obsolete or over-burdensome provisions in alcohol legislation have already been repealed, and early next year, the Government will introduce a radically reformed system for guaranteeing deferred payments of excise duty to deliver significant savings for compliant businesses.
- International shopping** **5.124** The Government welcomes the recent decision by EU Member States to double the tax-free allowance for international travellers returning from trips outside the EU, with a further review in four years time. **The new allowance of £290 applies to goods for personal use** (excluding tobacco and alcohol products which have separate quantitative limits) and is expected to take effect next year. The increase follows calls by the Government for a higher limit to better reflect modern shopping habits of EU citizens, reduce the burdens on international travellers and allow customs authorities to focus on their key priorities of facilitating trade and combating large scale fraud. New limits on excise goods, for international travellers returning from trips outside the EU, have also been agreed, with an increase from 2 to 4 litres for still wine and a limit on beer set at 16 litres. Limits on perfume, coffee and tea will be abolished.

Protecting tax revenues

5.125 A fair and effective tax system depends on everyone paying their fair share of tax and receiving only those benefits to which they are entitled. While the vast majority of companies and individuals interact with the tax and benefit system in this way, a small minority do not. Such tax avoidance and tax fraud undermine the ability of the system to deliver its objectives, imposing significant costs on the rest of society. The Government's strategic approach to

tackling avoidance, evasion and fraud is based on the principles of fairness and customer focus, ensuring that actions are tailored to the needs and behaviours of different taxpayers.

Tackling tax avoidance 5.126 To enable the Government to respond to avoidance more swiftly and in a more targeted fashion, Budget 2004 introduced a disclosure regime. In order to ensure that the regime functions consistently, the Government will **consult on a new power to investigate a scheme where there are reasonable grounds to believe that a promoter has failed to comply with its statutory disclosure obligations.**

5.127 Legislation, effective from today, will also be introduced to tackle a number of artificial schemes used by companies to avoid tax that have been notified under the disclosure regulations. The Government is also removing the public quotation exemption from the Controlled Foreign Companies regime to prevent specific avoidance.

Sale of lessors 5.128 As announced on 22 November 2006, and effective from that date, **legislation will be included in Finance Bill 2007, to tackle avoidance schemes that undermine the effect of the provisions on the sale of lessor companies introduced in Finance Act 2006.**

Structured finance 5.129 A measure to tackle avoidance involving structured finance schemes was announced on 6 June 2006 and enacted in Finance Act 2006.

Stamp duty land tax 5.130 This Pre-Budget Report **announces the introduction of secondary legislation, effective from 2pm today, to counter stamp duty land tax avoidance, including a number of known schemes using partnerships, sub-sales and leases.**

Capital gains tax 5.131 The Government is **introducing a measure effective from today that will prevent people creating and using capital losses purely to gain a tax advantage.** This measure will encompass the existing provision for companies included in this year's Finance Act without changing its effect.

Life insurance companies 5.132 **Legislation will be introduced effective from today to ensure that a transaction involving the transfer by life insurers of assets valued according to regulatory principles does not have inappropriate tax consequences.**

MTIC: VAT fraud 5.133 Missing Trader Intra-Community (MTIC) VAT fraud is a large-scale organised criminal attack on the EU VAT system, with the aim of creating large unpaid VAT liabilities and fraudulent VAT repayment claims. The scale of the attack on the VAT system increased in the latter part of 2005-06 and the first quarter of 2006-07, largely in response to a European Court case²⁷ that created legal uncertainty and removed one of HMRC's arguments used to deny suspect VAT repayment claims. New estimates published today²⁸ show that the scale of attempted MTIC fraud was between £3.5 billion and £4.75 billion in 2005-06; with an estimated negative impact on VAT receipts during the year of between £2 billion and £3 billion.

5.134 HMRC took proportionate steps to strengthen its operational response to MTIC fraud during 2005-06, including working with other law enforcement agencies to identify and destabilise the criminals behind the fraud and secure a number of convictions; and building a strong evidence base of the goods, people and tactics used in MTIC fraud. These measures helped to mitigate the impact on VAT receipts in 2005-06, though HMRC was obliged to repay suspect claims in the absence of sufficient evidence and robust legal arguments to deny them. However, a significant proportion of attempted frauds are now being stopped and the strengthened operational strategy has greatly reduced the level of attack, as reflected in the rapid fall in missing imports reported in ONS trade statistics.²⁹ Further legal rulings have

²⁷ The joined case of Bond House Systems Ltd and others (C-484/03, C-354/03, C-355/03).

²⁸ *Measuring Indirect Tax Losses – 2006*, HM Revenue and Customs, December 2006.

²⁹ *Balance of Trade in Goods*, ONS, November 2006.

provided HMRC with a strengthened basis to deny suspect VAT claims. This, together with the re-deployment of over 600 extra staff during 2006-07, mean that the vast majority of suspect repayment claims are now subject to in-depth checking and will not be paid unless and until found to be properly payable. HMRC is also pursuing monies previously paid out where there are suspicions they were associated with fraud.

5.135 The Government is determined to sustain the impact of its strategy and to ensure that HMRC has the tools it needs to combat MTIC fraud. **A further 100 HMRC staff are being redeployed to MTIC strategy, bringing the total to 1500.** As part of its wider strategy of working internationally to combat cross-border fraud, the Government is continuing negotiations with its European partners to secure the introduction of a reverse charge VAT accounting system for goods most commonly used in MTIC frauds. Further legislative measures will be brought forward in Budget 2007 as required.

Reform of VAT low value consignment relief **5.136** The Government continues to monitor the £18 VAT-free threshold for imports of small consignments from outside the EU. Despite the attempts of the Channel Island authorities to limit the exploitation of these rules, the cost of this relief has increased in the last six months to around £90 million per annum. The Government will assess the case for reform to protect tax revenues and will take into account the wider public interest, by balancing the compliance costs on carriers and importers with the impact on UK based retailers.

Tackling tobacco smuggling **5.137** Budget 2006 announced the Government's reinforced strategy for tackling tobacco smuggling. To enhance this strategy, and to tackle the growing problem of counterfeit tobacco, the Government has been working closely with the tobacco industry to identify measures to deal with this threat.

Tackling alcohol fraud **5.138** To tackle spirits fraud, the Government introduced the duty stamps scheme in October 2006. From 1 January 2007 all qualifying spirits sold in the UK must bear a UK duty stamp. However, there are signs that fraudsters are already changing their methods in response to this new environment, and the Government is discussing with the alcohol industry ways to tackle the emerging threat from counterfeit spirits.

Oils fraud **5.139** In the 2004 and 2005 Pre-Budget Reports, the Government announced that it would decrease the differential between rebated oil and main road fuel duties, in support of the oils strategy to combat fraud. HMRC is making good progress to reduce oils fraud to 2 per cent of the diesel market by 2006 and following Budget 2006, discussions with users of rebated gas oil have also provided a deeper evidence base on which to consider future decisions. This Pre-Budget Report announces that, with effect from midnight today, as originally announced in Budget 2006, **rebated oils rates will rise to maintain the differential with main fuel duties.** Further Government action to facilitate the use of biofuel/rebated oil mixes is outlined in Chapter 7.

5.140 HMRC continues to work closely with industry to identify and deal with potential risk areas within oils fraud. New controls have been introduced for aviation turbine fuel this year and HMRC will consult on proposals on the supply of marine fuels and on a potential risk-based relaxation of registered dealers in controlled oils (RDCO) requirements for small compliant suppliers. Following consultation, the Government announced in Budget 2006 proposed changes to the schedule of excepted vehicles entitled to use rebated gas oil, in order to achieve greater consistency and clarity. **The Government has today laid a draft Treasury Order amending the Schedule.**

Energy Products Directive derogations **5.141** The UK has a number of derogations from the Energy Products Directive that enable some oils to be charged duty at a reduced rate. These derogations are due to expire at the end of 2006. The Government has applied to the European Commission for an extension of the

derogations for fuel used in private air and pleasure craft navigation, and waste oils reused as fuel, drawing attention in particular to the significant enforcement, regulatory and administrative burdens of withdrawing the derogations. The Commission has declined to renew the derogation on private air navigation. The Government will consider options for legislating the change so as to ensure a suitable period of transition and to minimise the longer-term compliance burden. The Government is yet to receive a response on private pleasure craft and waste oils.

TACKLING GLOBAL POVERTY

Delivering the 2005 commitments **5.142** The commitments made by the EU and the G8 in 2005 on aid, trade, debt relief and governance were important steps towards helping the poorest countries achieve the Millennium Development Goals (MDGs). The focus now has to be on international delivery. While debt relief commitments are being delivered, challenges remain in other areas. The Government's 2004 Spending Review announced that the Department for International Development's (DfID) budget will grow from £3.8 billion in 2004-05 to £5.3 billion in 2007-08, an increase in real terms of 140 per cent since 1997. In 2006, the UK has also taken specific steps towards providing universal primary education (MDG 2) and through the International Finance Facility for Immunisation (IFFIm), combating communicable disease (MDGs 4 and 6). The UK is today taking further steps to improve research and development that supports the MDGs.

Access to healthcare **5.143** Better population health is a prerequisite for developing countries to break out of the cycle of poverty. Many of the major causes of ill health and mortality can be prevented and treated with known and affordable technologies. Many developing countries face a challenge in providing a basic package of healthcare in an environment of severe under-funding and shortages of trained health workers in which barriers to increased take-up of services, like user fees, limit poor people's access. The UK is committed to increasing spending on basic services (education, health, water and sanitation, and social protection) to 50 per cent of our bilateral aid programme by 2010-11. In addition, the UK is also committed to working with developing countries to back ambitious long-term plans to strengthen health systems and help partner governments abolish user fees for basic health services.

HIV/AIDS **5.144** The HIV/AIDS pandemic risks undermining progress towards the MDGs. The UK is strongly committed to achieving the goal – set at the 2005 G7 Finance Ministers and Gleneagles G8 Summit and confirmed by the UN in June 2006 – of universal access to comprehensive HIV prevention, treatment and care by 2010 and has pledged £1.5 billion to AIDS programmes in the three years up to 2008. Strengthening basic health systems, improving access to affordable medicines and improving education, particularly for girls, are critical to success. The UK also supports the long-term replenishment of the Global Fund for AIDS, TB and malaria (GFATM). The UK welcomes the announcement by Germany that tackling HIV/AIDS will be a priority for its G8 Presidency. We will continue to work with the G8 and the wider international community to meet the goal to combat HIV/AIDS.

Research and development **5.145** At present, only 10 per cent of global research and development on health is targeted on diseases that affect 90 per cent of the world's population. The UK Government will double development research funding by 2010, including increased funding for a new generation of drugs and vaccines, particularly through public-private partnerships (PPP). The UK has also led international efforts, with Canada and Italy, to establish a \$1.5 billion Advance Market Commitment (AMC), as a means of harnessing greater private sector investment and expertise into research and development for vaccines against diseases that kill millions in developing countries each year. We are committed to the launch of a pilot AMC for a

Pneumococcus vaccine in early 2007. Pneumococcal disease kills 1.6 million people a year, of which nearly a million are children. A successful AMC would save 5.4 million lives by 2030. The UK believes that AMCs have the potential to accelerate the discovery of vaccines against other killer diseases like Malaria and AIDS.

Collaboration in UK development sciences **5.146** The UK has played a leading international role in promoting policies to help the poorest countries achieve the MDGs. The best policies are firmly rooted in excellent research. The impact of scientific research in the international development context would be strengthened by improved coordination between funders. However, scientific research to cover medical, environmental, agricultural and other aspects of development could be better coordinated to further the UK's contribution to eradicating poverty and disease. By maximising the focus, quality and impact of UK research, we can leverage improved responses to the challenges of meeting the MDGs. Greater collaboration and coordination between the major bodies supporting UK scientific research in the development context will help attain this goal. That is why the Secretary of State for International Development is today announcing **the establishment of a research collaborative for the development sciences**. The collaborative will be led by a high level steering board including leading scientists from the Research Councils, the Wellcome Trust and Government departments that fund development science, and supported by the Gates Foundation in an advisory capacity.

Innovative finance for development **5.147** In 2005 the UK launched an International Finance Facility for immunisation (IFFIm) in partnership with several other donors, which will save an estimated 10 million lives in the poorest countries. The UK has also made a long-term financial commitment over a 20 year period to support an international drug purchase facility, UNITAID, which will help supply poor countries with lower-cost life-saving medicines for AIDS, tuberculosis and malaria. The UK contribution to UNITAID will start at €20 million (around £15 million) in 2007 and, subject to performance, gradually rise to €60 million (around £40 million) by 2011.

Box 5.6 The International Finance Facility for Immunisation

Worldwide, 2-3 million children under the age of five die every year from diseases for which we have, or soon will have, a vaccine. The GAVI Alliance (formerly the Global Alliance for Vaccines and Immunisation) was set up in 2000 to address this. Since 2000, GAVI has immunised over 115 million children and saved 1.7 million lives.

IFFIm was launched by the UK in September 2005 to enable GAVI to significantly expand its immunisation programmes. It will use the capital markets to convert long-term legally binding commitments from donors (UK, France, Italy, Spain, Sweden, Norway, South Africa, Brazil) into up-front resources for development. This frontloading will provide in over 70 of the poorest countries an additional \$4 billion to GAVI over the next ten years, immunising an extra 500 million children in the poorest countries and saving 10 million lives, including 5 million children by 2015.

On 7 November 2006, the inaugural bond issue for IFFIm was concluded, raising \$1 billion to purchase life-saving vaccines for children. As a gesture of solidarity the first six bonds were individually bought by His Holiness Pope Benedict XVI, the Archbishop of Canterbury, the Chief Rabbi, the Muslim Council of Britain, the Hindu Forum of Britain and the Network of Sikh Organisations. The remaining bonds were 1.75 times oversubscribed.

There are strong health and economic reasons for frontloading resources for immunisation. Early immunisation supports 'herd immunity'. When a child is vaccinated, it not only reduces the risk of him/her catching the disease, but also reduces the risk to others who come in contact with the child. This prevents the spread of disease and many more lives are saved faster.

Education 5.148 Education is one of the most cost effective investments that a country can make to support long-term development, enhancing economic growth as well as health outcomes. There has been some progress towards the education MDGs but not enough. Every day almost 80 million primary school-aged children are denied an education. If the education MDGs are to be achieved, out-of-school children must be enrolled by 2008. Developing countries need long-term predictable financing to enable investment in schools and teaching materials and to train teachers to deliver quality education. That is why the UK has announced that it will **spend at least £8.5 billion (\$15 billion) on aid for education over the next ten years and that, for the first time, it will enter into ten-year agreements to help countries finance their education plans.** The UK will continue to call on donors to deliver on their promises and provide long-term predictable financing to support countries' education plans and to achieve the education MDGs.

5.149 Many developing countries are already building on their existing education plans to prepare comprehensive and costed long-term plans to break the cycle of under-investment in education and meet the MDGs. In May, at the Abuja Financing for Development conference, 22 African countries committed to develop ten-year education plans. Following this, in September 2006, at a Ministerial Roundtable on Education at the IMF/World Bank Meetings in Singapore, seventeen African countries presented their progress on developing 10-year education plans. Fully developed and implemented, these plans would secure primary education for an additional 25 million children. At the Ministerial Roundtable, the UK called for an international donor conference on education in 2007, which the European Commission will host.

5.150 Nowhere is the importance of education, both to individuals and to society, more clearly demonstrated than through educating girls. Girls' education has a positive impact on individual's livelihoods, reducing rates of child mortality and HIV and AIDS infection as well as improving the nutrition and subsequent welfare of future generations. However, girls are more likely to be out of school and the UK is therefore calling on countries to include measures to improve the deliver of girls' education in their education plans.

5.151 Children in conflict are also particularly vulnerable. Approximately 39 million children – half of the world's children who are denied a primary school education – live in countries affected by conflict. Education in the midst of conflict can provide an important mechanism for the registration of young children and protection against abuse and can help states to recover from conflict. The UK will work with donor partners, developing countries and international agencies to strengthen the delivery of education to children affected by conflict.

Debt relief 5.152 The experience of the last ten years of the Heavily Indebted Poor Countries (HIPC) Initiative has shown that debt relief can be an extremely effective tool in support of poverty reduction. Under the HIPC initiative the debt burden of the world's poorest countries is being reduced over time by some \$60 billion, allowing the savings from debt relief to fund country-owned strategies aimed at reducing poverty. The recent decision by the World Bank and International Monetary Fund (IMF) to remove the sunset clause of the HIPC Initiative will enable all potentially eligible countries to benefit from HIPC debt relief.

5.153 The agreement on the Multilateral Debt Relief Initiative in 2005 will see the debts of 38 HIPCs to the IMF and concessional lending arms of the World Bank and the African Development Bank reduced by over \$50 billion. Debt relief worth \$38 billion is now being delivered to the 20 countries that have completed the HIPC Initiative. The UK also attaches great importance to extending multilateral debt relief to all of the poorest countries, not just those countries deemed eligible under the HIPC Initiative. The UK will therefore continue to pay its share of the debt service owed to the World Bank and African Development Bank by

other low-income countries that meet criteria for ensuring that the debt service savings are used for poverty-reduction. The UK urges other donor countries to agree to deeper debt relief for all low-income countries.

United Nations reform 5.154 The Government welcomes the report of the Secretary General's High Level Panel for System-wide Coherence in the areas of Development, Humanitarian Assistance and the Environment, on which the Chancellor served. The report³⁰ sets out a series of ambitious but achievable recommendations to improve performance, efficiency, accountability and results within the UN system; to enhance the voice of developing countries; to establish an empowered gender agency; to enhance the UN's role in responding to humanitarian disasters; and to reform the governance of environmental activities to improve their effectiveness. The report provides a clear vision of how the UN should act as one with much stronger coordination between its agencies, and coherence should be improved at headquarters, with action taken to avoid duplication and overlapping mandates. The Government will work with all stakeholders to implement the recommendations of the report as a matter of priority.

Trade 5.155 Under the right circumstances, trade can be a key driver of economic growth, development and poverty reduction. In the face of a current rise in protectionist sentiment, urgent reform of the global trading system is needed. The UK was extremely disappointed by the suspension of negotiations in the Doha Round of world trade talks this July and is calling for an urgent resumption and conclusion of full negotiations. Key World Trade Organisation (WTO) players need to show bold and concerted leadership to revive the talks and deliver significant increases in market access for developing countries, end export subsidies, substantially reduce all trade-distorting domestic support, and provide effective special and differential treatment to enable developing countries to capture the gains from trade. Developing countries must also have the flexibility to design, plan and sequence trade reforms in line with their country-owned development and poverty reduction strategies.

Aid for trade 5.156 Efforts to open markets and phase out subsidies will only generate a limited supply-side response from poorer countries unless they are complemented by the necessary investments to boost their capacity to trade, to help them participate effectively and fairly in the global trading system. Before the WTO ministerial in Hong Kong in December 2005, developed countries made 'aid for trade' pledges and agreed to prioritise investments in infrastructure. At the Annual Meetings of the IMF and the World Bank in Singapore this September, the UK announced that its support for 'aid for trade', which includes training trade specialists and building trade institutions, as well as support for infrastructure – like roads, ports, and telecommunications – is expected to increase by 50 per cent by 2010-11. This will equate to \$750 million a year in 2010.

5.157 Together European countries and the European Commission will increase assistance to a total of €2 billion a year by 2010. Japan has also promised \$10 billion over three years and the US a total of \$2.7 billion a year by 2010. The UK calls for all countries to turn their commitments into concrete and credible financing, within a new 'aid for trade' framework that cuts red tape and builds the infrastructure that businesses in poor countries need to compete.

Climate change 5.158 The Stern Review highlights that it is the poorest countries and people that are most vulnerable to the effects of climate change. Climate change will have serious effects on agriculture, water supply and health, posing a major obstacle to continued growth and poverty reduction in developing countries. Alongside international action to reduce greenhouse gas emissions, support is needed to help the poorest countries adapt to climate

³⁰ The full report can be downloaded at: <http://www.un.org/events/panel/resources/pdfs/HLP-SWC-FinalReport.pdf>

risks, so that the changing climate does not undermine poverty reduction. The UK welcomes the UN Secretary General's announcement at the Nairobi conference in November of steps to help developing countries – especially those in Africa – participate in the Kyoto Protocol's Clean Development Mechanism.

5.159 The UK has already contributed £10 million over three years to two funds agreed by the UN Framework Convention on Climate Change (UNFCCC) Parties: the Special Climate Change Fund (SCCF) and the Least Developed Countries Fund for Climate Change (LDCF). The UK is committed to mainstreaming climate risk reduction into development activities by DfID and multilateral organisations. We already have schemes underway to improve the quality and availability of climate risk data in Africa, and more widely to develop coherent approaches to climate risk screening and assessment. In addition the UK, with Canadian International Development Research Centre, has initiated a £30 million change research programme for 2006-2010, focusing on Africa.

Emergency relief 5.160 The UK Government has played a leading role in seeking international agreement to create the UN Central Emergency Relief Fund (CERF), which will have its own budget to enable the UN to respond immediately and substantially in the aftermath of a disaster, without waiting for donor pledges. The UK is the single largest donor so far with a contribution of £40 million, and has committed to giving £40 million a year over the next three years, making a total commitment £160 million. In addition, the UK has already contributed £50 million to a new IMF Shocks Facility to help reconstruction in countries ravaged by natural disasters or hit by commodity shocks.

5.161 Peace is the first condition for successful development and the Government will continue to support peacekeeping operations. The UK committed an additional £20 million to the African Union Mission in Darfur in February this year, bringing the total UK contribution to £52 million. Since September 2003 the UK has also provided over £126 million in humanitarian assistance to Sudan. The UK aim to work with others in the international community to support Sudan to reach a lasting peace, lay the foundations for sustained poverty reduction and begin to make progress towards the achievement of the MDGS. In 2006-07 the UK will be donating £110 million to Sudan.

5.162 As a member of the Core Group for Lebanon, the UK is actively supporting the Government of Lebanon in its efforts to recover from the crisis, reconstruct its economy and carry out the necessary reforms to ensure growth and stability in the future. The UK has contributed £22.3 million to meet priority relief needs to cover bridge repairs, humanitarian assistance, water sanitation and mine clearing. The UK will continue to provide support and expertise to the Government of Lebanon in the run-up to the reconstruction donor conference, which will take place in Paris in January 2007.

Reconstruction in Iraq 5.163 By the end of 2006, the UK will have disbursed the £544 million pledged in March 2003 for reconstruction in Iraq. In November 2006, the UK pledged a further £100 million over three years for economic regeneration. In addition, the UK and international partners continue to work alongside the Iraqi Government to support the December 2005 Stand-By Arrangement, Iraq's current IMF programme, which was successfully reviewed in August 2006 by the IMF Board.