



Government plans to extend childcare benefit to 2.5 million working parents

New tax-free childcare scheme will not depend on employers' participation

Access to affordable childcare looks set to be a key area of debate in the run up to next year's general election. In the recent Queen's Speech, the government confirmed its plan to reform and expand existing childcare benefits with the creation of a new "tax-free childcare" scheme.

Under the existing Employer Supported Childcare (ESC) scheme, working parents can receive up to £243 a month from their employers towards the cost of childcare, without deductions for tax or NI contributions having to be made. The payments, known as 'childcare vouchers', are paid to external administrators who then pass them on to childcare providers. Although the vouchers can be provided in addition to an employee's normal salary, in practice most employers participating in the scheme provide them by way of a salary sacrifice arrangement. This means that the employee elects to exchange part of his or her salary for childcare vouchers and benefits from the tax and NI savings that this provides. The employer also benefits from a reduced bill for employer NI contributions.

Take-up

Although ESC has been popular with employees, it appears to have been somewhat harder to persuade employers of the benefits of the scheme. Figures published by HMRC suggest that only about 5 per cent of businesses have chosen to offer it to staff. This could, in part, be due to concerns about the additional cost of providing childcare vouchers when an employee is on maternity leave.

When a woman is on maternity leave her employer must continue to provide her with any non-cash benefits to which she is entitled, and the cost of providing these cannot be offset against statutory maternity pay. Guidance published by HMRC makes clear that it regards childcare vouchers as non-cash benefits and not wages or salary (which employers do not have to continue to pay). As a result, employers offering childcare vouchers have to pay considerable additional sums for employees on maternity leave – unlike business that do not participate in the scheme.

Eligibility

Under the proposed new tax-free childcare scheme, working families will be able to claim 20 per cent of childcare costs up to a maximum of £2,000 per child. The benefit will not be available to families where at least one parent has annual earnings of £150,000 or more. It will be offered for children under five from autumn 2015 but children under 12 will then be covered within the first year. Unlike ESC, the self-employed will also be able to participate. Whether the new scheme turns out to be a better deal for parents will likely depend on the level of their spend on childcare. It looks as though large families requiring full-time childcare will potentially gain most.

The new scheme will not depend on participation by employers and will not impose any additional costs on businesses when employees are on maternity leave. However, it will not deliver NI savings as no salary sacrifice arrangement will be involved.

Potential outcomes

The introduction of tax-free childcare is expected to offer significantly more working parents the opportunity to obtain financial assistance with childcare costs. The government reckons that, once fully up and running, it will be open to around 2.5 million families, as compared to around 500,000 families under the existing scheme. Although some concerns have been expressed that the new scheme is likely to fuel demand for childcare and so drive up prices, for the most part the proposals have been welcomed. But whether they actually come to fruition might well depend on which party is in power after the general election.

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