HM Treasury

Cutting the 10% tax rate on savings income

The government announced at Budget 2014 that from April 2015, it is abolishing the 10% 'starting-rate' of tax for savings income and replacing it with a new 0% rate, to provide further support for the lowest earners.

It is also increasing the amount of savings income that the new 0% rate applies to, from £2,880 to £5,000. This means that anyone with a total income of less than £15,500 will not pay any tax on their savings.

What does the new 0% rate mean for me?

From April 2015, if your total income (things like wages, pension, benefits and savings income) is less than your personal allowance, plus £5,000, you will be eligible to register for tax-free savings, with your bank or building society.

Nearly everyone is entitled to a personal allowance, which allows you to receive a certain amount of income that isn't taxed. From April 2015, the basic tax-free personal allowance will be £10,500.

Non-savings income is always taxed before savings income. So the tax-free £5,000 savings band only applies if you earn less than £15,500 a year, or if some of your savings income falls into the £5000 that sits on top of your personal allowance.

Case studies

Case study: Derek

From April 2015 Derek will earn £12,000 a year in his part-time job as a gardener. His tax-free personal allowance is £10,500, so he is taxed at 20% (the basic rate of income tax), on £1,500 of his wages. He then earns £400 a year in savings income (interest earned on his savings). When you add up Derek's earnings and his savings income it equals less that £15,500, so Derek is eligible to register for tax-free savings.

How do I apply for tax-free savings?

Ask your bank or building society to pay your savings interest tax-free by filling in a R85 form. Download 'Form R85 – Apply for tax-free interest on your savings'.

Case study: Claire

From April 2015, Claire will earn £25,000 in her job as a chef. Her tax-free personal allowance is £10,500, so she is taxed at 20% on £14,500 of her wages. Claire also earns £300 a year in savings income. However as Claire earns over £15,500, her savings income is also taxed at 20%.

Case study: Sharon

From April 2015, Sharon will receive £14,000 per year from her pension. Her tax-free personal allowance is £10,500, so she is taxed at 20% on £3,500. Sharon also earns £2,000 a year in savings income. Sharon's total income is £16,000. Because Sharon's total income is more than her personal allowance plus £5000, she is not eligible to register for tax-free savings, but will be able to claim back some of the tax on her savings income. She can do this by filling out an R40 form and sending it to HMRC.

Download 'Form R40 – Claim back tax on your savings'.

If both Sharon and Claire's total income is over £15,500 – why is Sharon able to claim some of the tax back on her savings, but Claire isn't? Because the 0% tax-free savings band of £5,000 only applies if you are not filling all of your £15,500 with non-savings income.