HM Revenue & Customs

The starting rate of tax for savings

Who is likely to be affected?

Low income individuals who have taxable savings income (such as bank or building society interest).

Deposit takers (such as banks) and building societies.

General description of the measure

From 6 April 2015, the maximum amount of an eligible individual's savings income that can qualify for the starting rate of tax for savings will be increased to £5,000, and this starting rate will be reduced from 10 per cent to nil. This will increase the number of savers who are not required to pay tax on savings income, such as bank or building society interest.

Policy objective

This measure is part of a broader package of changes to support savers. In particular, it will enable savers with low incomes, and many people who depend on savings income, to retain more of their savings income. It will also simplify the current process around the starting rate for savings, removing the need for many eligible savers to reclaim tax from HM Revenue & Customs (HMRC).

Background to the measures

These measures were announced at Budget 2014.

Detailed proposal

Operative date

The measures will have effect on and after 6 April 2015.

Current law

Section 6 of the Income Tax Act 2007 (ITA 2007) provides three main rates of income tax. Section 7 specifies a 10 per cent rate for savings income - the starting rate for savings - which applies in defined circumstances.

Section 10(2) confirms that the first slice of an individual's taxable income is charged at the basic rate, unless it is alternatively charged by section 12 at the starting rate for savings. Section 12(1) provides that income tax is charged at the starting rate for savings on an individual's annual savings income up to the starting rate limit for savings.

Section 16 provides the ordering rules which determine at what rate income is taxable. Sections 16(3) to (5) provide that dividend income is the top part of an individual's taxable income (it is taxed last), savings income the middle part, and other income the lowest part (it is taxed first). The effect is that, should an individual's taxable non-savings income in a year exceed the starting rate limit for savings, the starting rate for savings will not apply. However, should their taxable non-savings income in a year be less than the starting rate limit, this savings income will be taxable at the starting rate, up to the starting rate limit.

Section 17 allows a tax repayment claim outside Self Assessment if a person has suffered tax at the basic rate on income liable to tax at the starting rate for savings. Currently, the starting rate for savings may be claimed by eligible savers making a reclaim to HMRC, where they have overpaid tax on their savings income.

Section 18 defines savings income. This includes various types of income in addition to bank and building society interest, such as gains on life insurance policies and income from purchased life annuities.

Section 21 includes indexation provisions for the starting rate limit for savings.

Section 851 requires deposit-takers (such as banks) and building societies to deduct sums representing basic rate income tax from certain interest payments. Section 852 allows HMRC to make regulations disapplying section 851 in certain circumstances. These include where a saver supplies a certificate to the bank or building society declaring that they are unlikely to be liable to pay any income tax for the year. The Regulations made under this provision are the Income Tax (Deposit–takers and Building Societies) (Interest Payments) Regulations 2008 (2008/2682).

Proposed revisions

Legislation will be introduced in Finance Bill 2014 to amend ITA 2007. It will reduce the starting rate for savings at section 7 to nil, and increase the annual starting rate limit for savings at section 12 to £5,000. It will also provide that indexation of the starting rate limit for savings (as provided for at section 21) will be disapplied for 2015-16.

Section 852 of ITA 2007 will be updated to allow regulations to provide that deduction of sums representing income tax on interest payments will not be required where a saver provides a certificate declaring they are unlikely to be liable to pay income tax on their savings income for the year.

Following Royal Assent to Finance Bill 2014, changes will be made to the Income Tax (Deposit–takers and Building Societies) (Interest Payments) Regulations 2008 by secondary legislation. This will enable savers to register with their bank and building society to receive interest payments without tax deducted if all of their savings income is eligible for the starting rate. This will remove the need for many savers to make a reclaim to HMRC in relation to tax amounts deducted from interest payments.

Summary of impacts

<table>
<tr><td rowspan="3">Exchequer impact (£m)</td><td>2014-15</td><td>2015-16</td><td>2016-17</td><td>2017-18</td><td>2018-19</td></tr>
<tr><td>-</td><td>-135</td><td>-320</td><td>-325</td><td>-355</td></tr>
<tr><td colspan="5">These figures are set out in Table 2.1 of Budget 2014 and have been certified by the Office for Budget Responsibility. More details can be found in the policy costings document published alongside the Budget.</td></tr>
<tr><td>Economic impact</td><td colspan="5">These measures will reduce income tax on savings for some low income individuals, improving incentives to save and increasing real household disposable incomes. This might feed through to higher consumption or savings in the household sector.</td></tr>
<tr><td>Impact on individuals and households</td><td colspan="5">The Government expects around 1.5 million individuals to potentially benefit from a tax reduction on their savings income, and around half of these individuals to benefit by more than £50 per year. It estimates that over one million individuals will no longer be liable for tax on any of their savings income as a result of this change. Allowing eligible savers to register with a bank or building society for interest to be paid gross (without tax deducted) will remove the need for many to reclaim tax from HMRC, and will therefore provide a significant simplification. As well as savers with low overall incomes, this measure will also benefit some individuals with average or higher incomes whose income is primarily interest on savings.</td></tr>
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Equalities impacts	The change will primarily benefit those with low overall incomes - typically pensioners, part time workers, and non-working adults with savings income that takes them above the personal allowance. Around 40 per cent of those benefitting are expected to be pensioners, 185,000 of whom would be entirely taken out of tax. This measure will also benefit some individuals with average or higher incomes whose income is primarily interest on savings. No other impacts are anticipated in respect of groups with protected characteristics.
Impact on business including civil society organisations	The Government anticipates that banks and building societies could receive requests for account interest to be paid gross, from up to 900,000 additional savers. This will require them to undertake the one-off process of registering the request. However, banks and building societies already have well-established and simple processes in place and the overall impact on businesses is expected to be negligible. This measure is expected to have no impact on civil society organisations.
Operational impact (£m) (HMRC or other)	The additional costs/savings for HMRC in implementing this change are not expected to be significant.
Other impacts	<u>Small and micro business assessment</u>: no major issues specific to smaller businesses have been identified. Other impacts have been considered and none have been identified.

Monitoring and evaluation

This measure will be kept under review through communication with affected taxpayer groups and account providers.

Further advice

If you have any questions about this change, please contact Simon Turner on 03000 546588 (email: simon.turner@hmrc.gsi.gov.uk).