Government Actuary's Department

The Right Honourable
Shabana Mahmood MP
Lord Chancellor & Secretary of State for Justice
102 Petty France
London
SW1H 9AJ

Fiona Dunsire
Government Actuary, Chair of the PIDR Expert Panel
6th Floor
10 South Colonnade
London
E14 4PU

7 November 2024

Fiona.Dunsire@gad.gov.uk

Dear Lord Chancellor,

Subject: Impact of capital gains tax rate increase on the Personal Injury Discount Rate advice

I am writing on behalf of the Expert Panel to discuss the impact of the changes to capital gains tax rates announced in the Autumn Budget on our advice in relation to the Personal Injury Discount Rate.

Increases to capital gains tax rates are to take effect from April 2025, with the basic rate increasing from 10% to 18% and the higher rate increasing from 20% to 24%. This is expected to increase the tax costs for personal injury claimants, which in turn would reduce their net investment return and reduce the likelihood of reaching specified compensation levels under a given Personal Injury Discount Rate.

The Expert Panel has commissioned the Government Actuary's Department to assess the impact of these higher tax rates on outcomes for the three core claimant types and the corresponding levels of under- or over-compensation at different Personal Injury Discount Rates.

As set out below, from the analysis we conclude that the impact of the higher tax rates is negligible and does not change our advice or materially change the figures presented in our report.

The 20-year core claimant is expected to pay very little capital gains tax over their investment term since much, or all, of their capital gains in each year fall under the tax-free allowance. The increase in capital gains tax rates has virtually no impact on their median net return or their likelihood of achieving at least sufficient compensation.

The 40-year and 60-year core claimants are expected to pay more capital gains tax over the term, however, for both claimant types, the median net return decreases by less than 0.05%.

Since the impact is less than 0.05%, the advice in our report dated 25 September 2024 still stands and does not need amending as a result of the capital gains tax rate increases.

I continue to be available to assist with your deliberations in any way required.

Yours sincerely,

Fiona Dunsire
Government Actuary, Chair of the PIDR Expert Panel

Government Actuary's Department

PIDR: Impact of higher capital gains tax rates announced in Autumn Budget

5 November 2024

This report has been prepared by GAD for the Ministry of Justice (MOJ) and the Expert Panel. The purpose of the report is to discuss the impact on key claimant outcomes of higher capital gains tax (CGT) rates announced in the Autumn Budget on 30 October 2024. This report should be considered in conjunction with the GAD Analytical Report.

Summary

Higher CGT rates as announced in the Autumn Budget do not materially reduce the median net returns or the likelihoods of at least sufficient compensation for the three core claimants.

Tax changes

The analysis in the GAD Analytical Report was based on the tax structure for the 2024/25 tax year. At the Autumn Budget changes to capital gains tax rates were announced that will be in force from April 2025, with the basic rate increasing from 10% to 18% and the higher rate increasing from 20% to 24%.

The table below shows the existing tax rates assumed in the original analysis and the new tax rates. No changes were announced to the tax rates for income/savings or dividends, or to the tax-free allowances, so we have only changed the CGT rate assumptions.

Tax type	Existing tax rates	New tax rates
Income/savings tax	Basic: 20% Higher: 40% Additional: 45%	(unchanged)
Capital gains tax	Basic: 10% Higher: 20%	Basic: 18% Higher: 24%
Dividend tax	Basic: 8.75% Higher: 33.75% Additional: 39.35%	(unchanged)

Impact on core claimant outcomes

Higher CGT will have an impact on claimants who earn capital gains above the tax-free allowances in a given tax year. The level of capital gains depends mainly on the fund size but also on the investment portfolio, the returns on the portfolio, and other taxable income.

The impact of the higher CGT rates is that a claimant's tax costs in any given year is either unchanged (where any capital gain is assumed to be within the threshold and no CGT is paid) or increased (where capital gain is assumed to be above the threshold and CGT is paid). The increase will be to a greater proportion where the basic rate is assumed to be paid since the percentage increase is larger. Over the whole term, a claimant's net investment return would either be unchanged or decreased.

The table below shows the average annual tax drag over the investment term under the existing and new CGT rates for the three core claimant types (20-year, 40-year, 60-year).

Core claimant type	Lump sum size	Tax drag p.a.		
		Existing	New	Change
20-year	£500k	0.32%	0.32%	**+0.00%**
40-year	£1m	0.21%	0.25%	**+0.04%**
60-year	£5m	1.17%	1.21%	**+0.04%**

Assuming no change to investment returns or expenses, the decrease in median net return is assumed to be equal to the increase in tax drag. The median net return would be virtually unchanged for the 20-year core claimant, and would reduce by less than 0.05% for the 40-year and 60-year core claimant types.

The impact of likelihoods of achieving different levels of compensation is also minimal. In particular, the likelihood of achieving at least sufficient (100%) compensation is unchanged for the 20-year core claimant and reduces by around 1% for the 40-year and 60-year core claimants.

Therefore, higher CGT rates as announced in the Autumn Budget do not materially change the key outcomes for the three core claimants. We believe the advice in the GAD's Analytical Report and the Expert Panel's report to the Lord Chancellor remains appropriate.

The 20-year core claimant is expected to pay very little CGT over their investment term since much, or all, of their capital gains in each year fall under the tax-free allowance. The impact of higher CGT rates is therefore negligible.

The 40-year and 60-year core claimants are expected to pay more CGT over the term relative to their initial lump sum size, since their lump sums are larger and more of their capital gains are above the tax-free allowance. But the increase in CGT rates does not materially reduce their net investment return.

Limitations of the analysis

The limitations set out in the GAD Analytical Report also apply to this analysis.

We have made no changes to other assumptions from the GAD Analytical Report, such as expenses or investment returns. Higher CGT rates may have a wider impact on the investment returns available or the expenses charged but we are assuming that this is not material to this advice.

Tax management beyond full ISA utilisation is not modelled in either the GAD Analytical Report or this analysis, though in practice claimants are likely to look to reduce their tax drag where possible. The announced increase in CGT rates could lead to claimants to take measures to reduce CGT (e.g. by investing in different asset classes) and we have not made any allowance for this.

Compliance

This report has been prepared for the use of MOJ and the Expert Panel and must not be reproduced, distributed, or communicated in whole or in part to any other person without GAD's prior written permission.

Other than MOJ or the Expert Panel, no person or third party is entitled to place any reliance on the contents of this report, except to any extent explicitly stated herein. GAD has no liability to any person or third party for any action taken or for any failure to act, either in whole or in part, on the basis of this report.

This work has been carried out in accordance with the applicable Technical Actuarial Standard: TAS 100 issued by the Financial Reporting Council (FRC). The FRC sets technical standards for actuarial work in the UK.