

## **Taxation of Savings – what can you have tax-free?**

There is no one answer to the amount of savings income and, for 2017/18, the answer can range from £0 to £18,650, depending on personal circumstance

When looking at tax-free savings, there are a number of elements to take into account:

- the personal allowance;
- the marriage allowance;
- the savings allowance; and
- the starting rate for savings.

Savings income, such as bank and building society interest, is now paid gross without tax deducted.

### **Personal allowance**

If a person has no other income (or only dividend income in addition to savings income), or their other income is less than £11,500, some or all of the personal allowance (set at £11,500 for 2017/18) will be available to shelter savings income.

### **Marriage allowance**

Where the marriage allowance is claimed, this increases the potential tax-free income by £1,150 in 2017/18.

### **Savings allowance**

In addition to the personal allowance, individuals who pay tax at the basic or higher rate are also entitled to a savings allowance. The amount of the allowance depends on the individual's marginal rate of tax and is set at £1,000 a year for basic rate taxpayers and at £500 a year for higher rate taxpayers. There is no savings allowance for additional rate taxpayers.

### **Savings starting rate**

Savers with little in the way of other taxable income can also benefit from a 0% savings starting rate on savings of up to £5,000, in addition to savings sheltered by the personal and savings allowance. However, the savings starting rate is quite complicated in that the starting rate limit is reduced by taxable non-savings income. So, if a person has taxable non-savings income of £2,000, the savings starting rate of 0% is available on savings income of £3,000, as the £5,000 limit is reduced by the taxable non-savings income of £2,000 to £3,000. Likewise, if a person has taxable non-savings income of more than £5,000, the savings starting rate limit is reduced to nil.

### **Case study 1: maximum tax-free savings**

Elsie is retired and her only income is savings income, which in 2017/18 is £20,000. Her husband has income of £8,000 and Elsie benefits from the marriage allowance of £1,150. The first £11,500 of her savings income is covered by her personal allowance of £11,500 and the next £1,150 by the marriage allowance, leaving £7,350, of which £1,000 is covered by the personal savings allowance for basic rate taxpayers. This leaves savings income of £6,350. As she has no taxable non-savings income, she is entitled to the savings starting rate of 0% on savings equal to the saving starting rate limit of £5,000. Consequently, she is able to enjoy £18,650 (£11,500 + £1,150 + £1,000 + £5,000) of her savings tax-free and is taxed at the basic rate of 20% on her remaining savings of £1,350 – giving her a tax bill of £270.

### **Case study 2: reduced starting rate limit**

In 2017/18, Arthur has a pension of £14,000 and savings income of £6,000.

His personal allowance is set against his pension, leaving him with taxable non-savings income of £2,500.

He is entitled to the saving personal allowance of £1,000, which is set against £1,000 of his savings income.

As he has taxable non-savings income of less than £5,000, the savings starting rate is reduced by his taxable non-savings income of £2,500 to £2,500. £2,500 of his savings income is eligible for the 0% savings starting rate.

He, therefore, receives savings income of £3,500 tax-free. The remaining £2,500 of his savings income is taxed at 20%, as is the excess of his pension over his personal allowance of £2,500. His tax bill for 2017/18 is, therefore, £1,000 (£5,000 @ 20%).

### **Case study 3: higher rate taxpayer**

Wendy has a salary of £50,000 and savings income of £5,000 in 2017/18. Her personal allowance is set against her salary. She is entitled to the personal savings allowance of £500 available to higher rate taxpayers, but she is not eligible for the savings starting rate as her taxable non-savings income (£38,500, being £50,000 - £11,500) is more than £5,000. She receives tax-free savings income of £500.

As the case studies show, the amount of savings income a person may receive can vary considerably depending on what other income they have and the rate at which they pay tax.