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BRIEFING PAPER

Number 8870, 6 April 2020

Direct taxes: rates and allowances 2020/21

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Contents:

Contents

Summary

This paper sets out direct tax rates and principal tax allowances for the 2020/21 tax year, as announced in the 2020 Budget on 11 March 2020. The paper outlines the conditions necessary for eligibility for these tax allowances, and provides a summary of the general tax position in straightforward cases.

Income tax on earned income is charged at three rates: the basic rate, the higher rate and the additional rate. For 2020/21 these three rates are 20%, 40% and 45% respectively. Tax is charged on taxable income at the basic rate up to the basic rate limit, set at £37,500. 'Taxable income' excludes personal allowances, which represent the amount of money someone may receive free of tax. Tax is charged at the higher rate on taxable income between the basic rate limit and the higher rate limit, set at £150,000. The additional rate is charged on taxable income over £150,000. All three tax rates are unchanged from 2019/20.

The **personal allowance** is set at £12,500 for 2020/21, unchanged from the year before. The basic rate limit is also unchanged for 2020/21, so that the higher rate threshold – the point at which individuals become liable to pay tax at the higher rate – remains at £50,000 for 2020/21.

In the 2012 Budget the Coalition Government announced it would phase out the two **age-related personal allowances**, claimed by individuals aged 65-74, and those aged 75 and over. Both allowances have now been overtaken by the personal allowance and have been withdrawn.

In the 2015 Budget the Coalition Government confirmed the introduction of a new **marriage allowance**. From April 2015 individuals whose income is insufficient to make full use of their personal allowance may transfer this unused fraction to their spouse or civil partner, up to a set amount. Individuals cannot make use of this provision if their spouse or partner pays more than the basic rate of tax. For 2020/21 the maximum that can be transferred remains set at £1,250.

The rates of **National Insurance contributions** (NICs) for both employees and employers are unchanged for 2020/21. For employees, the rate of NICs is set at 12% on all earnings between the primary threshold and the upper earnings limit, and at 2% on earnings above the upper earnings limit. For employers, the rate of NICs is set at 13.8% on earnings above the secondary threshold. The primary threshold is set at £183 per week, and the secondary threshold is set at £169 per week for 2020/21. The upper earnings limit is set at £962 per week for 2020/21, so that it remains aligned with the income tax higher rate threshold.

This paper deals with tax allowances, but not with cash benefits provided under the social security system, or child tax credit and working tax credit. Details of these credits, along with other tax rates and allowances for the 2020/21 year are set out in Annex A to HM Treasury, *Overview of Tax Legislation and Rates*, March 2020 published alongside the 2020 Budget report.

1. Rates and thresholds

1.1 Income tax

Income from earnings, pensions, profits

All 'non-savings' income – income from earnings, pensions, taxable social security benefits, trading profits and income from property – are subject to income tax at the same rates.

For 2020/21 income tax on these categories of income is charged at three rates: the basic rate of 20%, the higher rate of 40% and the additional rate of 45%. All three rates are unchanged from 2019/20.

The 20% basic rate applies to taxable income up to a threshold of £37,500. Taxable income excludes personal allowances, which represent the amount of money someone may receive free of tax. (Personal allowances are discussed in section 2 of this paper.)

Taxable income in excess of the threshold is charged at the higher rate of 40%, up to £150,000. Income earned above this threshold is charged tax at 45%.

2019/20		2020/21	
Taxable income	**Tax rate**	**Taxable income**	**Tax rate**
£0 - £37,500	**20%**	**£0 - £37,500**	**20%**
£37,501 - £150,000	**40%**	**£37,501 - £150,000**	**40%**
Over £150,000	**45%**	**Over £150,000**	**45%**

A 10% starting rate of tax used to apply on non-savings income, but was withdrawn in April 2008.

Two new allowances which apply to income from property and income from trading were introduced from April 2017. Individuals with property income or trading income below the level of the allowance do not need to declare this income or pay tax on it. Both allowances are set at £1,000 for 2020/21.[1]

Scottish taxpayers

From 2017/18 the Scottish Government has had the power to set all income tax rates and thresholds to apply to Scottish taxpayers' non-savings and non-dividend income. The Scottish Government does not have the power to set the level of the income tax personal allowance.

For 2020/21 the Scottish Government has set five rate of income tax: the starter rate of 19%; the basic rate of 20%; the intermediate rate of 21%; the higher rate of 41%; and the top rate of 45%. It has also set the four thresholds at which these rates take effect.

1 HMRC, *Tax-free allowances on property and trading income*, May 2019. see also, Low Incomes Tax Reform Group, *What is the trading allowance?*, 10 January 2020 & *Renting out a property*, 23 March 2020

These rates and thresholds are set out below – the table assumes someone is in receipt of the UK personal allowance:[2]

Taxable income	**Tax rate**
Over £12,500 - £14,585	**19%**
Over £14,585 - £25,158	**20%**
Over £25,158 - £43,430	**21%**
Over £43,430 - £150,000	**41%**
Above £150,000*	**46%**

* Personal Allowance is reduced by £1 for every £2 earned over £100,000

Savings and dividend income

For 2020/21 savings income is charged at 0% for income up to £5,000. Above this limit savings income is charged tax at the basic rate of 20%, up to the basic rate limit of £37,500. Savings income above this limit is charged at the 40% higher rate, up to the higher rate limit of £150,000. Savings income above this limit is charged at the 45% additional rate.

Since April 2016 savers have been entitled to claim a new Personal Savings Allowance (PSA). This applies a 0% rate for up to £1,000 of savings income for basic rate taxpayers. The allowance applies a 0% rate for up to £500 of savings income for higher rate taxpayers. Additional rate taxpayers are not eligible for the allowance. Historically savings income has been taxed at source by banks and building societies at 20%. Alongside the introduction of the PSA, automatic deduction of tax at source was withdrawn.[3]

For 2020/21 dividend income is charged at 0% for income up to £2,000 – the Dividend Allowance. Above this limit dividend income is charged tax at a basic rate of 7.5%, up to the basic rate limit. Dividend income above this limit is charged at a higher rate of 32.5%, up to the higher rate limit. Dividend income above this limit is charged at an additional rate of 38.1%.

In calculating tax liability, dividend and savings income are regarded as the 'top slice' of income, with dividends the highest.[4]

2 The Scottish Government publishes details of these rates and thresholds on its site.
3 For more details see, HMRC, *Tax on savings interest*, ret'd March 2020
4 See also, Low Incomes Tax Reform Group, *Savings and tax*, 24 March 2020

1.2 National Insurance contributions

Employees are liable to Class 1 (primary) National Insurance contributions (NICs) on their earnings if they exceed the lower earnings limit (LEL). The LEL is set at £120 per week for 2020/21.

However, a zero rate of NICs is charged on earnings between the LEL and the primary threshold (PT), which is set at £183 per week. A notional primary Class 1 NIC is deemed to have been paid in respect of earnings between LEL and PT to protect benefit entitlement. Earnings above the PT are charged NICs at a rate of 12%, subject to a cap at the upper earnings limit (UEL), which is set at £962 per week. Earnings *above* the UEL are charged NICs at a rate of 2%.

Prior to 6 April 2016 employees were charged a reduced rate of NICs if they had contracted out of the state second pension (S2P). These arrangements have ended with the introduction of the 'single-tier' state pension, and the closure of the additional state pension, from this date.[5]

Employers pay Class 1 (secondary) NICs on employee earnings at a rate of 13.8% on earnings above the secondary threshold (ST). The ST is set at £169 a week for 2020/21.

Employers may be entitled to one of three tax reliefs on their payment of employer NICs.

First, in the 2013 Budget the Government announced the introduction of a new **Employment Allowance** – a flat rate deduction for businesses and charities against their annual employer NICs bill, to apply from April 2014.[6] Initially the Allowance was set at £2,000, but was increased to £3,000 from April 2016, and is set to rise to £4,000 from April 2020.[7] From April 2020 the Allowance may only be claimed by employers with an employer NICs below £100,000 in their previous tax year, a change announced in the 2018 Budget.[8] Further details on the operation of the Allowance are published by HMRC.[9]

Second, in the 2013 Autumn Statement the Government announced an **Upper Secondary Threshold (UST) for under 21s** from April 2015.[10] From his date a zero rate has applied to earnings on this category of employee up to the UST set in line with the UEL.

In the 2014 Autumn Statement the Government announced an **Apprentice Upper Secondary Threshold (AUST)** from April 2016.[11]

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5 For details see, *The new State Pension: transitional issues*, Commons Library Briefing paper CBP7414, 25 February 2019.

6 *Budget 2013*, HC 1033, March 2013 para 2.41. Statutory provision for the new allowance was made by ss1-8 of the *National Insurance Contributions Act 2014.*

7 These increases in the Allowance were made by Order: SI 2016/63, and, SI 2020/273

8 *Budget 2018*, HC 1629, October 2018 para 3.11. This change was made by Order : SI 2020/218; see also, HMRC, *Employment Allowance: excluded persons regulations 2020*, 24 January 2020

9 HMRC, *Employment Allowance*, retrieved March 2020

10 *Autumn Statement*, Cm 8747, December 2013 para 1.195. Statutory provision for the UST by s9 of the *National Insurance Contributions Act 2014.*

11 *Autumn Statement*, Cm 8961, December 2014 para 2.53. Statutory provision for the AUST was made by s1 of the *National Insurance Contributions Act 2015.*

From this date a zero rate has also applied to earnings on this second category of employees up to the AUST, also aligned with the UEL.

The UST and AUST are set at £962 per week for 2020/21.

Class 1 NICs rates for employees and employers for 2020/21

Earnings[a] £ per week	**Employee NIC rate (per cent)**	**Earnings £ per week**	**Employer NIC rate (per cent)**
Below £120 (LEL)	0%	Below £120 (LEL)	0%
£120 to £183 (PT)	0%	£120 to £169 (ST)	0%
£183 to £962 (UEL)	12%	Above £169	13.8%
Above £962	2%		

[a] *The limits are defined as LEL - lower earnings limit; PT - primary threshold; ST - secondary threshold; and UEL - upper earnings limit.* [12]

Self-employed people pay a weekly flat rate Class 2 NIC (set at £3.05). They may apply for exemption from paying Class 2 contributions if their annual profits are less than the level of the 'small profits threshold' (SPT), set at £6,475. In addition they may be liable to pay a separate Class 4 profits related contribution. Class 4 NICs are charged at a rate of 9% on profits between a lower annual profits limit (£9,500) and an annual upper profits limit (£50,000 – all figures for 2020/21). Profits above the upper limit are charged NICs at a rate of 2%.

Further to these categories, individuals may be entitled to make voluntary Class 3 contributions to ensure that they qualify for the state pension and bereavement benefits. Class 3 NICs are charged at a weekly flat rate, set at £15.30 for 2020/21.[13]

[12] HM Treasury, *Budget 2020: overview of tax legislation and rates*, March 2020 (Annex A: Rates and Allowances). These thresholds are set by Order (SI 2020/299).

[13] For more details on the operation of NICs see, *National Insurance contributions: an introduction*, Commons Briefing paper CBP4517, 16 December 2019.

2. Income tax allowances

All individuals are entitled to claim a personal allowance which they can set against income tax. An allowance is also given to individuals who are blind.

2.1 Personal allowance

Every taxpayer resident in the United Kingdom is entitled to a **personal allowance** that can be set against any type of income for tax purposes. For 2020/21 this allowance is £12,500.

In May 2010, the Coalition Government announced that over the 2010-15 Parliament it would substantially increase the personal allowance, set at £6,475 for 2010/11, up to £10,000. The allowance was increased each year, to reach £10,000 for 2014/15.[14] In the Conservative Government's first Budget after the 2015 General Election, the then Chancellor George Osborne pledged to increase the allowance to £12,500 and the higher rate threshold to £50,000, by the end of the Parliament.[15] In the 2018 Budget the Chancellor Philip Hammond confirmed that the personal allowance and higher rate threshold would be set at £12,500 and £50,000 respectively for 2019/20. The then Chancellor went on to state that both would be frozen for 2020/21, and then increased in line with CPI inflation from 2021/22.[16]

Since April 2010 the personal allowance has been withdrawn from individuals whose incomes exceed £100,000. The allowance is reduced by £1 for every £2 above this income limit, until completely withdrawn. This income limit is unchanged for 2020/21.

2.2 Blind person's allowance

Any person registered as blind is entitled to the **blind person's allowance**. The allowance is set at £2,500 for 2020/21. If someone has insufficient income to make use of the allowance it can be transferred to their spouse or civil partner.

2.3 Transferable allowance for married couples & civil partners

Individuals whose income is insufficient to make full use of their personal allowance may transfer a fraction of the allowance to their spouse or civil partner, up to a set amount. Individuals cannot make use of the transferable tax allowance for married couples and civil partners – or, **marriage allowance**, as it is known – if their spouse or partner is

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14 For more details see, *Income tax : increases in the personal allowance since 2010,* Commons Briefing paper CBP6569, 15 November 2018.
15 HC Deb 8 July 2015 c336; *Summer Budget 2015*, HC246, July 2015 paras 1.130-4
16 HC Deb 29 October 2018 cc667-8; *Budget 2018*, HC1629, October 2018 para 3.7. This was confirmed in Budget 2020 (*Budget 2020 Policy Costings*, March 2020 p63).

liable to tax above the basic rate of tax. The allowance was introduced in April 2015. For 2020/21 the maximum that can be transferred is £1,250. In effect the recipient is entitled to a tax credit worth up to £250 to set against their tax bill.

Individuals who may wish to apply to have part of their allowance transferred in this way to their partner may register with HMRC either online or by phone. Eligible couples can backdate their claim for the allowance for up to four years.[17] In the Autumn 2017 Budget the Government announced that claims for the allowance would be allowed in cases where a partner has died before the claim was made, and that these claims would be able to be backdated by up to 4 years.[18]

2.4 Indexation

For many years income tax legislation has required the main personal allowances and income tax thresholds to be increased in line with the Retail Prices Index (RPI) unless Parliament determines otherwise.

This statutory requirement - the so-called "Rooker-Wise" amendment - was introduced under section 22 of the *Finance Act 1977*.[19] The amendment was successfully made through the cross-party co-operation of Jeff Rooker, Audrey Wise and Nigel Lawson. All three argued that without indexation, inflation acted as an unauthorised, unintended and unknown increase in taxation. By requiring that any real changes in allowances would be voted on, the amendment ensured that changes in the income tax structure would be 'out in the open'. Indeed, for many years since then, allowances went up in line with inflation or by more than inflation.[20]

In the 2011 Budget the Coalition Government announced that from April 2012 the default indexation assumption for direct taxes would be the Consumer Price Index (CPI), though RPI would be retained for some allowances and thresholds for the duration of the 2010 Parliament.[21] This approach was amended in the light of three measures: the phased withdrawal of the age-related allowances for taxpayers from April 2013; the increase in the personal allowance in 'real terms' – by more than inflation – in both 2014/15 and 2015/16; and, the increase in the higher rate threshold by 1% in the first of those years.

Any elements of the direct tax system that were indexed by reference to RPI are covered by CPI.[22] The threshold for the additional rate (£150,000), and the income limit for the tapered withdrawal of the

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17 HMRC, *Marriage allowance*, ret'd March 2020. HMRC's helpline is 0300 200 3300. See also, PQ14045, 3 November 2015; PQ HL4734, 30 January 2017.

18 *Autumn Budget 2017*, HC587, November 2017 para 3.6. See also, *Income tax allowances for married couples*, CBP870, 9 September 2019.

19 The statutory requirement to uprate allowances and thresholds, is consolidated in sections 57 & 21 of the *Income Tax Act 2007*, as amended

20 HL Deb 7 January 2010 c121WA

21 *Budget 2011*, HC 836, March 2011 para 1.128. see also, Office of National Statistics, *Users and uses of consumer price inflation statistics*, October 2016

22 HM Treasury, *2020 Budget : policy costings*, March 2020 pp63-7 (Annex A: Indexation in the public forecast baseline).

personal allowance (£100,000), have not been included in these provisions, and are fixed in monetary value.

When uprating the main allowances and thresholds, the relevant inflation rate is the increase in inflation in the year to September, prior to the start of the following tax year.[23] When allowances and thresholds are increased in line with inflation, they are rounded up to the nearest £10 or £100. For personal allowances, this income limit is £10; for the basic rate limit, it is £100. CPI rose by 1.7% in the year to September 2019.[24]

2.5 Age-related allowances (withdrawn)

Prior to 2013/14, individuals were entitled to claim one of two age-related additions to the personal allowance, if they were aged between 65 and 74 years of age, or were 75 or over. The allowance was withdrawn if an individual's income exceeded a set limit. This was done by cutting the allowance by £1 for every £2 by which an individual's income exceeded a set income limit.

In the 2012 Budget the Coalition Government announced that from April 2013 both allowances would be phased out: each allowance would be frozen in cash terms, until they became aligned with the personal allowance. In addition, only existing recipients would be entitled to claim either allowance. At this time these allowances were frozen at £10,500 (for taxpayers born after 5 April 1938 but before 6 April 1948), and £10,660 (for taxpayers born before 6 April 1938).[25]

From 2016/17 both age-related allowances have been overtaken by the personal allowance and have been withdrawn. Taxpayers that were claiming these allowances are now eligible for the 'basic' personal allowance.

2.6 Transitional allowances for older people

Four allowances were withdrawn from April 2000: the married couple's allowance (MCA) for couples aged under 65 at that time; the additional personal allowance; the maintenance allowance for separated or divorced couples under 65; and the widow's bereavement allowance.[26]

The MCA and tax relief on maintenance payments were retained for individuals where either they, or their current or former spouse, had reached the age of 65 by the start of the tax year 2000/01; i.e., they were born on or before 5 April 1935.

[23] for details see, HM Treasury, *Tax benefit reference manual: 2009-2010 edition*, July 2009, paras 1.16-19. [HC DEP 2009-1987]
[24] ONS, *UK Consumer Price Inflation: September 2019*, October 2019
[25] For more details see, *Age-related personal allowance*, CBP6158, 11 May 2016.
[26] This measure was announced in the March 1999 Budget; see, *Direct taxes: rates & allowances 2000/01*, Commons Research paper RP00/38, 29 March 2000 pp11-12.

Married couple's allowance

Married couples, in which at least one partner reached 65 by 6 April 2000, are still entitled to claim a **married couple's allowance**.[27] For 2020/21, this allowance is set at £9,075, increased in line with inflation. Tax relief for the allowance is 'restricted' to 10%. In effect taxpayers receive a credit worth 10% of the MCA to set against their final tax bill: ie, £908.

The value of the MCA is gradually reduced for taxpayers earning above an income limit, in the same way as the age-related personal allowances were (see above). For 2020/21 this income limit is set at £30,200. The withdrawal of the MCA from older couples is subject to a minimum allowance set at £3,510 for 2020/21, restricted to 10%. No couple entitled to the allowance will receive less than this.

Where a couple marry during the tax year the allowance is reduced by one twelfth for each complete tax month pre-marriage. In the first instance the MCA is given to the husband, though if couples elect to do so, the minimum MCA can be transferred to the wife or split equally between spouses. In previous years, in line with the personal allowance, an age-related MCA was given to couples aged between 65 and 74, and a second, higher MCA to those 75 or over. Given that anyone who reached 65 by 6 April 2000 will be 86 or over this tax year, it is only the second of these allowances that remains applicable.

Civil partners may also claim the MCA provided – as with married couples – at least one partner was born before 6 April 1935.[28]

Tax relief for maintenance payments

Generally, maintenance payments are made outside the tax system: those who make payments cannot claim them against tax, and those who receive them are not taxed on them. Separated or divorced individuals who pay maintenance direct to their ex-spouse under a legally binding agreement may qualify for a limited form of tax relief – often referred to as a '**maintenance allowance**' – provided that one or more of the parties reached 65 prior to 6 April 2000. This relief is set equal to the 'minimum' MCA that couples can receive if they are now 86 or over (which is £3,510 restricted to 10% for 2020/21). Individuals who make maintenance payments to a child, or to someone to whom they have not been married, do not qualify for this relief. Tax relief is withdrawn if the ex-spouse who receives maintenance remarries.[29]

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27 When a person born on or before 5 April 1935 newly gets married, that person or their spouse is entitled to claim this allowance.

28 More guidance is given on Gov.uk. In March 2005 the then Labour Government announced that civil partners would be treated the same as married couples for tax purposes, when the *Civil Partnership Act 2004* came into force on 5 December 2005.

29 See also, Low Incomes Tax Reform Group, *What tax allowances am I entitled to?*, March 2020.

3. Income tax: other allowances & reliefs

3.1 Company cars & free fuel

Generally individuals are taxed on the cash value of any 'fringe benefit' they enjoy by virtue of their employment.

The cash value is added to their taxable income, and taxed accordingly; ie, taxed at the same rate as the rest of their income (20%, 40% or 45% depending on their circumstances). Some basic guidance on these rules is given on Gov.uk.

Special rules apply in evaluating the cash value of a company car. This is calculated as a percentage of the car's price – the 'appropriate percentage' – set by reference to the car's CO_2 emissions level, which is expressed in grams per kilometre (g/km).[30]

In the Autumn 2017 Budget the Government announced that from April 2020 the emissions test used to underpin company car tax, as well and vehicle excise duty (VED), would be the new Worldwide harmonised Light vehicles Test Procedure (WTTP).[31]

The new test is more rigorous, and initial evidence provided by manufacturers suggests that using the WLTP would mean that the reported emissions of over 50% of cars could rise by 10% to 20%. To smooth the transition, in July 2019 it was announced most CCT rates would be cut by 2% in 2020/21 for cars first registered from 6 April 2020.[32] Rates would return to planned levels over the next two years, increasing by 1% in 2021/22 and 1% in 2022/23. After this point rates are to be frozen until 2024/25.

Budget 2020 confirmed this measure, while setting out rates for cars registered *before* 6 April 2020.[33]

The taxable benefit of free fuel provided for private motoring in a company car is also calculated by reference related to the level of CO_2 emissions. To calculate the monetary value of this benefit, the 'appropriate percentage' is multiplied against a set figure for the year; for 2020/21 this is set at £24,500.[34]

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30 HMRC, *Expenses & benefits: a tax guide,* Notice 480, December 2019 (see Appendix 2)

31 HM Treasury, *Overview of tax legislation and rates*, November 2017 para 1.17

32 HM Treasury, *Review of WLTP and vehicle taxes: summary of responses*, July 2019

33 *Budget 2020*, HC 121, March 2020 para 2.227; HM Treasury, *Budget 2020: overview of tax legislation and rates*, March 2020 (Annex A: Rates and Allowances).

34 HMRC, *Income Tax changes to the van benefit charge and fuel benefit charges for cars and vans from 6 April 2020*, 11 March 2020. This multiplier is set by Order: SI 2020/199.

3.2 Pensions

The annual and lifetime allowances

Contributions to pensions are exempt from tax when made, but taxed when they are paid out to the individual. Pension contributions made by individual employees are usually paid out of pre-salary, so tax relief is received at the individual's marginal tax rate.

The main limits to this are:

- The annual allowance (AA) - is the most you can save in your pension pots in a tax year (6 April to 5 April) before you have to pay tax.[35]
- The lifetime allowance (LTA) - which limits the amount of pension saving over an individual's lifetime that can benefit from tax relief.[36]

Both limits were introduced in April 2006 under the *Finance Act 2004.*

At introduction in 2006, the AA was set at £215,000 and the LTA at £1.5 million.[37] Both allowances increased in stages, with the LTA reaching £1.8m and the AA £255,000 by 2010.[38]

Since 2010, they have been reduced on a number of occasions.

- The LTA reduced to £1.5m in 2012, to £1.25m in 2014 and to £1m in April 2016. The Government then legislated for it to be index-linked to inflation from 2018.[39] In April 2020, it will increase in line with the CPI from £1,055,000 to £1,073,100.[40]
- The standard AA was reduced to £50,000 in 2011 and then to £40,000 in 2014.
- From April 2016, there has been a tapered AA, which operates to reduce an individual's AA, by £1 for every £2 of 'adjusted income' (essentially, total taxable income plus the real growth in value of pension rights over the year) above a set level, down to a minimum of £10,000.

In 2019/20, there were many reports about the impact of the tapered AA on the NHS. Although the rules apply across pension schemes in the public and private sectors, the nature of the work – with senior clinicians taking on additional work, often at short notice, to cover service pressures – meant they had a particular impact in the NHS. Faced with potentially very large tax bills, doctors felt unable to take on that work.[41]

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35 *Finance Act (FA) 2004*, s227; HMRC, Pension Tax Manual – Annual Allowance.
36 *FA 2004*, s216; HMRC, Pension Tax Manual – Lifetime Allowance
37 *FA 2004* s218, s218 and 228
38 *Budget 2004*, HC 301, March 2004 para 5.45
39 *Budget 2015*, HC1093, March 2015, para 1.232
40 *Budget 2020*, HC 121, March 2020, para 2.186; *Finance Act 2016*, s19
41 BMA letter to Chancellor to the Exchequer, Philip Hamond, March 2019; DHSC consultation, July 2019; Pension tax driving doctors to retire early, Royal College of Physicians, October 2019; Royal College of Surgeons press release, 22 November 2019; NHS Providers, An unnecessary divide, Jan 2020

The Government announced in the Budget on 11 March 2020 that it would increase the threshold income levels at which the tapered AA applies:

- The threshold income, which is broadly net income before tax (excluding pension contributions), would increase from £110,000 to £200,000.
- The adjusted income, which is broadly net income plus pension accrual, would increase from £150,000 to £240,000.

It would also reduce the minimum AA from £10,000 to £4,000.[42]

The British Medical Association (BMA) welcomed the changes saying they would reduce the vast majority of doctors from the taper. However, it argued that the solution was long overdue and that the Government should have removed the AA from defined benefit schemes altogether, as had been suggested by the Office of Tax Simplification.[43] The Association of British Insurers (ABI) also thought more fundamental reform was needed.[44]

The last consultation on fundamental reform of pension tax relief in 2015, resulted in no change on the grounds that there had been "no consensus."[45]

For more detail, see

Commons Briefing Paper *Pension tax rules: impact on NHS consultants and GPs* (CBP 8626, March 2020).

Commons Briefing Paper *Reform of pension tax relief* (CBP 7505, February 2020).

Pension freedoms

In 2015, there were important changes to the the pension tax rules, giving people aged 55 and over more flexibility about when and how to draw their defined contribution (DC) pension savings (where people contribute to a fund which is invested and used to provide an income at retirement).[46]

Before this, most people with DC pensions effectively had to buy an annuity.[47] The advantage of annuities is that they provide a guaranteed income throughout retirement. However, their popularity had declined due to falling annuity rates and evidence that parts of the market did not work well for consumers.[48]

The Government introduced a limit of £10,000 on the annual amount an individual can save in a DC pension once they have accessed their savings flexibly. However, this was reduced to £4,000 from April 2017. The reason was to reduce the opportunity to 'recycle' pension savings

For more information, see

Commons Briefing Paper *Pension flexibilities: the freedom and choice reforms* (CBP 6891, December 2019).

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42 HMRC, *Pensions Tax Changes to income thresholds for calculating the tapered annual allowance from 6 April 2020*, 11 March 2020

43 BMA says Government has 'finally listened' to months of lobbying to fix pension taxation crisis and improve patient care, 11 March 2020; OTS, *Taxation and Life Events*, October 2019, chapter 3

44 ABI responds to Budget 2020, March 2020; Budget 2020, Professional Adviser, March 2020

45 HM Treasury, *Strengthening the incentive to save: reforming pension tax relief*, Cm 9102, July 2015; HC Deb 16 March 2016 c966; *Budget 2016*, HC901, March 2016, para 1.108-9.

46 HC Deb 19 March 2014 c794; *Budget 2014*, HC 1104, para 1.156-66; *Taxation of Pensions Act 2014*

47 HM Treasury, *Freedom and choice in pensions*, Cm 8835, March 2014, Diagram 3A

48 FSCP, *Annuities: Time for Regulatory Reform*, December 2013

while leaving some scope for people who need to access their savings, to subsequently rebuild them.[49]

The 'pension freedoms' are not available to people to have already purchased an annuity – because this is generally a one-off and irreversible purchase.[50] In its March 2015 Budget, the Coalition Government proposed allowing annuity holders to sell their income stream to a third party.[51] However, in October 2016, these plans were cancelled because it was clear that creating the conditions for a competitive market could not be balanced with consumer protections.[52]

The pension freedoms were not aimed at people defined benefit (DB) pensions, for whom staying in their scheme was likely to be in their best interest. This is because a DB scheme provides index-linked benefits based on salary and length of service, whereas in a DC scheme, your future pension income cannot be predicted with any certainty.[53] At the time, the Government realised that the pension freedoms could encourage more defined benefit (DB) scheme members to transfer their pensions into a DC scheme. It therefore introduced a mandatory financial advice requirement for those wishing to transfer or convert a DB pension worth more than £30,000 into a DC pension.[54]

3.3 Charities

There is no general tax exemption or relief granted to taxpayers who make gifts to charities. Tax relief is provided through two schemes which cover regular donations made out of one's salary (Payroll Giving) and one-off gifts (Gift Aid).

Under the **Payroll Giving** scheme charitable donations are wholly deductible for income tax purposes, the relief being given through the PAYE system. The employer deducts the appropriate sum from a participating employee's pay, and passes it to an agency which distributes it to the charity or charities of the employee's choice. There are no minimum or maximum limits for donations under the scheme.[55]

Gift Aid allows income tax relief for single donations by individuals. When this relief was introduced in 1990, a minimum limit on donations was set at £600. Subsequently this limit was cut to £250 before being abolished entirely from 6 April 2000. As a consequence, tax relief

49 *Autumn Statement 2016*, Cm 9362, November 2016, para 4.20; HM Treasury, *Reducing the money purchase annual allowance: consultation,* November 2016; *Finance (No. 2) Act 2017*, s7; HMRC, *Reducing the annual money purchase allowance*, 8 March 2017

50 Financial Conduct Authority, *Retirement income market study: Interim Report*, Executive Summary

51 *Budget 2015,* HC 1093,18 March 2015, paras 1.229-31

52 HM Treasury, Government cancels plans to create market for secondary annuities, 18 October 2016; PQ 49517, 26 October 2016). For more details see, *Secondary annuities market*, Commons Briefing Paper CBP7707, 4 November 2016.

53 Money and Pensions Service, Transferring out of a defined benefit pension scheme, ret'd April 2020.

54 *Pension Schemes Act 2015,* s48; HM Treasury, *Freedom and choice in pensions: government response to consultation*, July 2014, Foreword

55 A maximum limit of £1,200 a year applied prior to 6 April 2000.

applies to a donation of any size.[56] Under the scheme charities claim repayment of basic rate tax on donations. Higher rate taxpayers claim higher rate tax relief on their gifts.

In April 2013 the Government launched a scheme to allow charities to claim Gift Aid on small donations without a Gift Aid declaration. Under the **Gift Aid Small Donations Scheme** (GASDS) individual donations must be made in cash and be worth no more than £20. Charities may claim a top-up payment, equivalent to Gift Aid relief, on an annual maximum of donations. Initially this limit was set at £5,000 per year, but was increased to £8,000 from April 2016.[57] From April 2017 eligible donations may be made by contactless payment as well as in cash, one of a number of changes to simplify and increase access to the GASDS.[58] The cash limit on donations is increased to £30 from April 2019.[59]

56 Guidance for taxpayers on both payroll giving and Gift Aid is published on Gov.uk.
57 This change was made by Order: SI 2015/2027.
58 For more details see, *Gift Aid Small Donations Scheme*, CBP6330, 6 February 2019
59 This change was also made by Order: SI 2019/237.

4. Other direct taxes

4.1 Capital gains tax

Capital gains tax (CGT) is charged on gains in excess of the annual exempt amount, which is set at £12,300 for 2020/21. Individuals may realise gains up to this threshold free of tax. The tax is charged at a rate of 10%, and at 20% on gains realised by individuals paying income tax at the higher or additional rates. Gains from residential property not eligible for Private Residence Relief, and from carried interest, are liable to tax at higher rates: 18%, and 28% respectively.[60]

The structure of CGT rates was reformed by the Coalition Government in its first Budget in June 2010. Prior to this, gains had been subject to a single rate set at 18%, introduced as part of a series of reforms to CGT by the Labour Government in its 2008 Budget.[61] The new Government introduced a 28% rate for higher rate and additional rate taxpayers, with effect from Budget day (22 June 2010).

In the 2016 Budget the then Chancellor George Osborne announced that both rates of CGT would be cut, from 18% and 28%, to 10% and 20% respectively, from 6 April 2016. The rates of tax were left unchanged for gains from residential property not eligible for Private Residence Relief, and gains from carried interest.

Gains qualifying for entrepreneur's relief are charged a rate of 10%. A £10m lifetime limit has applied to capital gains qualifying for this relief since April 2011. In the 2020 Budget the Chancellor Rishi Sunak announced that the lifetime limit would be cut to £1m with immediate effect.[62] A 10% rate also applies to gains made by long term investors in unlisted companies, subject to a lifetime limit of £10m of gains.

4.2 Inheritance tax

Inheritance tax is levied on the value of a person's estate at the time of their death. Most large gifts made out of someone's estate within seven years of their death are treated as part of their estate for tax purposes. The tax is charged at 40% above the tax-free allowance, which is set at £325,000 for 2020/21.[63]

Gifts made to one's spouse or civil partner are exempt from tax irrespective of their size, and irrespective of whether they are made during one's life, or made under the terms of one's will. In addition, widows, widowers and civil partners are entitled to use the share, if any, of their partner's tax-free allowance which was unused when they died, to set against tax on their own estate. This transferable allowance is

60 Guidance on CGT is published on Gov.uk.
61 Prior to this capital gains were treated in the same way as the top slice of income, and the tax was charged at the same rates of tax as savings income.
62 *Budget 2020*, HC 121, March 2020 para 2.199; HMRC, *CGT Entrepreneurs' Relief - reduction in the lifetime limit*, 11 March 2020
63 Guidance on inheritance tax is published on Gov.uk.

available to all survivors of a marriage or civil partnership who die on or after 9 October 2007 – whenever their first partner died.

In the Summer 2015 Budget the then Chancellor George Osborne announced that from April 2017 an additional nil-rate band would apply on death to transfers of a main residence to a direct descendant.[64] In this context a direct descendant is "a child (including a step-child, adopted child or foster child) of the deceased and their lineal descendants."

The additional nil-rate band was set initially at £100,000 and is set at £175,000 for 2020/21.

In his Budget Mr Osborne also announced that the *existing* nil-rate band would be frozen at £325,000 at least until 2020/21, while the main residence nil-rate band would rise by £25,000 each year, to reach £175,000 in 2020/21.[65]

The additional nil-rate band is subject to a taper. For any estate with a net value of more than £2m, the band will be withdrawn by £1 for every £2 the estate exceeds this threshold. If someone downsizes or ceases to own a home before they die, the additional band may still be claimed on assets of an equivalent value, if passed on death to direct descendants. This is to apply if someone downsizes or ceases to own a home on or after 8 July 2015. As with the existing nil-rate band, any unused fraction of the main residence nil-rate band may be transferred to a surviving spouse or civil partner.[66]

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64 *Summer Budget 2015*, HC264, July 2015 paras 1.217-221; para 2.89

65 In 2013 the Coalition Government had proposed that the threshold should be frozen until April 2018 (*Budget 2013*, HC1033, March 2013 para 2.76.)

66 For details see, HMRC, *Inheritance tax: main residence nil-rate band and the existing nil-rate band*, updated June 2017

5. Main personal income tax rates & allowances since 1990/91

Table 1

Main income tax rates and allowances: 1990/91-2020/21

	Allowances/Limits (£ per annum)			Rates			
	Personal allowance	Lower/ Starting Rate Limit	Basic Rate Limit	Lower/ Starting	Basic	Higher	Additional
1990/91	3,005	n/a	20,700	n/a	25%	40%	n/a
1991/92	3,295	n/a	23,700	n/a	25%	40%	n/a
1992/93	3,445	2,000	23,700	20%	25%	40%	n/a
1993/94	3,445	2,500	23,700	20%	25%	40%	n/a
1994/95	3,445	3,000	23,700	20%	25%	40%	n/a
1995/96	3,525	3,200	24,300	20%	25%	40%	n/a
1996/97	3,765	3,900	25,500	20%	24%	40%	n/a
1997/98	4,045	4,100	26,100	20%	23%	40%	n/a
1998/99	4,195	4,300	27,100	20%	23%	40%	n/a
1999/00	4,335	1,500	28,000	10%	23%	40%	n/a
2000/01	4,385	1,520	28,400	10%	22%	40%	n/a
2001/02	4,535	1,880	29,400	10%	22%	40%	n/a
2002/03	4,615	1,920	29,900	10%	22%	40%	n/a
2003/04	4,615	1,960	30,500	10%	22%	40%	n/a
2004/05	4,745	2,020	31,400	10%	22%	40%	n/a
2005/06	4,895	2,090	32,400	10%	22%	40%	n/a
2006/07	5,035	2,150	33,300	10%	22%	40%	n/a
2007/08	5,225	2,230	34,600	10%	22%	40%	n/a
2008/09	6,035	n/a	34,800	n/a	20%	40%	n/a
2009/10	6,475	n/a	37,400	n/a	20%	40%	n/a
2010/11	6,475	n/a	37,400	n/a	20%	40%	50%
2011/12	7,475	n/a	35,000	n/a	20%	40%	50%
2012/13	8,105	n/a	34,370	n/a	20%	40%	50%
2013/14	9,440	n/a	32,010	n/a	20%	40%	45%
2014/15	10,000	n/a	31,865	n/a	20%	40%	45%
2015/16	10,600	n/a	31,785	n/a	20%	40%	45%
2016/17	11,000	n/a	32,000	n/a	20%	40%	45%
2017/18	11,500	n/a	33,500	n/a	20%	40%	45%
2018/19	11,850	n/a	34,500	n/a	20%	40%	45%
2019/20	12,500	n/a	37,500	n/a	20%	40%	45%
2020/21	12,500	n/a	37,500	n/a	20%	40%	45%

Notes (a) From 2008/09, a 10 per cent starting rate of income tax is retained for savings income. See text for further details.

Sources: HM Treasury, Budgets 2010 - 2020
Tax Benefit Reference Manual 2009-10,
HMRC. Budget 2020: overview of tax legislation and rates (OOTLAR)

Table 2
Age-related allowances: 1990/91 to 2020/21
£ per annum

	Personal (a)		Married couple's (b)	
	65-74	75+	65-74	75+
1990/91	3,670	3,820	2,145	2,185
1991/92	4,020	4,180	2,355	2,395
1992/93	4,200	4,370	2,465	2,505
1993/94	4,200	4,370	2,465	2,505
1994/95	4,200	4,370	2,665	2,705
1995/96	4,630	4,800	2,995	3,035
1996/97	4,910	5,090	3,115	3,155
1997/98	5,220	5,400	3,185	3,225
1998/99	5,410	5,600	3,305	3,345
1999/00	5,720	5,980	5,125	5,195
2000/01	5,790	6,050	5,185	5,255
2001/02	5,990	6,260	5,365	5,435
2002/03	6,100	6,370	5,465	5,535
2003/04	6,610	6,720	5,565	5,635
2004/05	6,830	6,950	5,725	5,795
2005/06	7,090	7,220	5,905	5,975
2006/07	7,280	7,420	6,065	6,135
2007/08	7,550	7,690	6,285	6,365
2008/09	9,030	9,180	6,535	6,625
2009/10	9,490	9,640	..	6,965
2010/11	9,490	9,640	..	6,965
2011/12	9,940	10,090	..	7,295
2012/13	10,500	10,660	..	7,705
2013/14	10,500	10,660	..	7,915
2014/15	10,500	10,660	..	8,165
2015/16	10,600	10,660	..	8,355
2016/17*	11,000	11,000	..	8,355
2017/18	11,500	11,500	..	8,445
2018/19	11,850	11,850	..	8,695
2019/20	12,500	12,500	..	8,915
2020/21	12,500	12,500	..	9,075

Notes: (a) from 2013/14 eligibility for the age-related allowances will be restricted to existing recipients

(b) Relief restricted to 20 per cent in 1994/95, 15 per cent from 1995/96 to 1998/99, and to 10 per cent from 1999/00.
Since 2000/01 the MCA has only been given to couples in which at least one partner was born before 6 April 1935.

* from 2016/17 age-related allowances have been merged with the personal allowance.

Sources: HM Treasury, Budgets 2010 - 2020
Tax Benefit Reference Manual 2009-10,
HMRC. Budget 2020: overview of tax legislation and rates (OOTLAR)

BRIEFING PAPER
Number 8870
6 April 2020

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