

Tax treatment of dividend income and personal savings income

Dividend income

The Dividend Tax Allowance (DTA) came into force on 6 April 2016, replacing the 'notional' tax credit previously attaching to net dividend payments. It has been set at a level of £2,000 per annum since 6 April 2018.

Dividend income above £2,000 is taxed at the following rates:

Basic rate tax payers	7.5%
Higher rate tax payers	32.5%
Additional rate tax payers	38.1%

After taking account of the available personal allowance (£12,500 for the tax year 2020/2021), everyone will be able to receive £2,000 of dividend income with no further tax implications. So for an individual with income of £14,500 or less, there will be no liability to tax on dividend income.

For those with income up to £50,000 (personal allowance plus entire basic rate tax band of £37,500 for 2020/21) there will be a maximum liability to tax on dividend income of £2,662.50 ((£37,500-£2,000) x 7.5%).

Where dividend income falls in the higher rate tax band (over £50,000) a dividend tax liability will be charged at 32.5%, and for the additional rate band (over £150,000) the rate increases to 38.1%.

Dividends are taxed as the top slice of income and so if an individual receives non dividend income that takes them into the higher or additional rate tax bands, they can still receive up to £2,000 of dividend income tax free.

Example

Nathan is employed and earns £48,500 per annum gross. He also receives dividends of £9,000 from an investment portfolio.

Gross earnings	48,500	
Less: Personal allowance	(12,500)	
	36,000	
Dividends up to basic rate band	1,500	Not taxable
	37,500	
Balance of dividend allowance	500	Not taxable
Dividend income taxable	7,000	Taxed at 32.5% - £2,275

There is an added complication for those earning over £100,000 as the personal allowance reduces by £1 for every £2 earned over £100,000.

Dividend income within an ISA remains unaffected by the changes, with no tax being due on such income.

The DTA does not apply to trusts, and a 38.1% rate of tax applies to the dividend income received by discretionary and accumulation trusts above the current standard rate band of £1,000. Dividends within the standard rate band are taxed at 7.5%.

Personal savings income

The Personal Savings Allowance (PSA) was introduced with effect from 6 April 2016 when banks and building societies stopped deducting 20% tax from interest payments.

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Continued

The allowance remains at a rate of £1,000 for basic rate taxpayers, and £500 for higher rate taxpayers. The allowance is not available for additional rate taxpayers and, again, does not apply to trusts. It should also be noted that this is not an additional exemption as the allowance is treated as part of the basic rate band.

The PSA applies to all interest bearing investments including treasury stocks, corporate bonds, interest yielding OEICs and gains from offshore investment bonds.

Individuals do not need to do anything to claim the PSA. Banks and building societies will pass details of interest credited to accounts to H M Revenue & Customs each year. PAYE coding notices will be updated to collect any tax due on interest over the allowance.

For those within self-assessment, interest received should still be included within the tax return, with any tax due on interest over the allowance being payable in January and July as previously.

Example

Sandra has a salary of £49,000, interest income of £1,000 and £20 of dividends. Gross income is over £50,000 reducing the PSA available to £500.

Earnings	Salary	Savings	Dividend
Gross	49,000	1,000	20
Personal Allowance	(12,500)		
Taxable	36,500	1,000	20
Basic rate band at 20%	7,300		
PSA £500 at 0%		0	

Basic rate band at 20%		100	
DTA £2,000 at 0%			0

In this example, it may be possible to make a gift aid payment to reduce income back down to under £50,000 and restore the PSA to £1,000 thus reducing the tax liability on savings income to £0.

For more help or information please contact:



Kristina Mathieson
Personal Tax Manager
T 01892 701232
E kristina.mathieson@ts-p.co.uk