**INCOME TAX**

**LECTURE 2**

**SLIDE 1 – INCOME TAX**

Hello, my name is Sarah Brooks. This online lecture relates to the subject area of taxation and is the second lecture on Income Tax.

**SLIDE 2 – OUTCOMES**

In this second online lecture, I am going to be focusing on the Income Tax calculation. I am going to explain how Income Tax is calculated and within that I shall be discussing how you calculate total income and net income. I shall also be explaining what the personal allowances are in relation to Income Tax.

**SLIDE 3 – INCOME TAX CALCULATION**

To calculate an individual’s Income Tax liability, you must work through the following five steps:

* Firstly, you will calculate their total income.
* Secondly, you will deduct any allowable reliefs to give a figure which is known as Net Income.
* Thirdly, from that Net Income figure you will deduct any personal allowances to give a figure which is known as Taxable Income.
* Fourthly, you will separate non savings & non dividend income (“NSNDI”), savings income and dividend income and tax at the appropriate rates.
* Finally, you will add together each of the figures from step 4.

It is important that whenever you are calculating Income Tax liability you ensure that you follow those five steps.

**SLIDE 4 – CALCULATING TOTAL INCOME**

The first stage in working out an individual’s Income Tax liability is to calculate their total income. Total income is calculated by simply adding together all the taxable sources of income received by that individual in the tax year. Remember taxable sources of income come from the Income Tax Trading and Other Income Act or the Income Tax Earnings and Pensions Act and cover such things as trading profits, salaries, interest on savings or rental income.

**SLIDE 5 – CALCULATING TOTAL INCOME – EXEMPT INCOME**

To calculate Total Income, you add together all of the taxable sources of income received by an individual in a tax year. It is important to note though that some sources of income are exempt from taxation. These are set out in Part 6 of the Income Tax Trading and Other Income Act and includes such things as income from investments in ISAs, benefits, interest on National Savings Certificates and interest on damages for personal injury or death.

**SLIDE 6 – CALCULATING TOTAL INCOME**

Now that I have explained to you how to calculate Total Income it is time for you to have a go. I would like you to calculate Total Income based on the following facts:

* James Evans owns and runs a small garden centre. In a given tax year he sells a small plot of land for £10,000; he sublets his basement flat for £6,000, trading profit is £30,000 and he also receives income from an ISA of £200.00. Have a go at calculating James’s Total Income.

I suggest that at this point you pause the online lecture, have a go at doing the calculation and then resume the online lecture when you have come up with a total income figure.

**SLIDE 7 – CALCULATING TOTAL INCOME**

Hopefully, you have calculated James’s Total Income as £36,000. Remember to calculate Total Income you add together all of James’s taxable sources of income. James had £30,000 trading profit which will be taxable under Part 2 of the Income Tax Trading and Other Income Act and he also had £6,000 from subletting his basement flat which would be taxable under Part 3 of the Income Tax Trading and Other Income Act. Added together then this gives James a Total Income of £36,000. The £10,000 that James received from selling the plot of land doesn’t need to be included in the Total Income calculation as this is a one-off sale and therefore is capital and not income and the £200.00, he received from his ISA is exempt income under Part 6 of the Income Tax Trading and Other Income Act and again isn’t included in the calculation.

**SLIDE 8 – CALCULATING NET INCOME**

The second stage in calculating any individual’s Income Tax liability is to calculate their Net Income. This is calculated by taking the Total Income figure that we have just looked at and deducting any allowable reliefs.

**SLIDE 9 – ALLOWABLE RELIEFS**

Allowable reliefs are amounts that HM Revenue and Customs will allow you to deduct from your Total Income in order to reduce your overall Income Tax liability. Allowable reliefs are interest on qualifying loans. This covers such things as interest on a loan to buy a share in a partnership, interest on a loan to invest in a close trading company or interest on a loan made to PRs to pay Inheritance Tax. It is important to note then that it is only the interest on these loans that can be deducted as an Allowable relief and it only covers these kinds of loans. Unfortunately, it doesn’t include interest on general bank loans or student loans.

**SLIDE 10 – CALCULATING TAXABLE INCOME**

The third stage in calculating an individual’s Income Tax liability is to calculate their taxable income. To do this then we take the net income that we have just talked about and deduct the individual’s personal allowance. This then gives the individual’s taxable income.

**SLIDE 11 – PERSONAL ALLOWANCES**

An individual’s personal allowance varies from year to year and is set by the Government in its Annual Budget. For the current tax year, the personal allowance can be seen on the slide. Please note though that an individual’s personal allowance can be more depending on the individual’s circumstances and is reduced if an individual has an income of over £100,000.

You can find details of these other personal allowances on the Government website but for the purposes of this course we will always work on the basis that the personal allowance is the most common one so the one shown on the slide.