**INCOME TAX**

**LECTURE 3 – SAVINGS AND DIVIDENDS**

**SLIDE 1**

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

**SLIDE 2 – OUTCOMES**

In this third online lecture I am going to be talking about the different rates at which income tax is paid and looking at an income tax calculation. Finally, I shall be talking about the dates an individual has to pay their income tax liability.

**SLIDE 3 – RATES OF TAX**

There are two main income tax rates, the basic rate and the higher rate. For the tax year 2022/23 the basic rate is paid on any taxable income which falls between 0 and £37,700. The higher rate is paid on taxable income that exceeds £37,701. Please note that there is third rate, the additional rate that applies to taxable income which exceeds £150,000.

It is important to note that when taxing income you must use up each of these bands in their entirety before moving on to the next. For example, if an individual’s taxable income was £38,000, the first £37,700 would be taxed at the basic rate and the remaining £300 would be taxed at the higher rate. Just because an individual’s taxable income is £38,000 it doesn’t mean it is all taxed at the higher rate. Finally, it is important to note that the percentage an individual pays on income that falls within each of those bands depends on the different type of income that is being taxed. Different percentages rates apply for non-savings and non-dividend income, interest on savings and dividends.

**SLIDE 4 – RATES OF TAX**

When taxing an individual’s non-savings, non-dividend income, in other words income that comes from their business or their employment, any income which falls within the basic rate of up to £37,700 is taxed at 20%. Income which falls within the higher rate is taxed at 40% and any income which falls within the additional rate is taxed at 45%.

**SLIDE 5 – RATES OF TAX - SAVINGS**

When taxing an individual’s income from interest on their savings the situation is slightly different. Although the basic, higher and additional rates are 20%, 40% and 45%, the same as they are for taxing non savings, non dividend income, the band for the basic rate is slightly different. If an individual has NSNDI of up to £5,000, any income that individual receives from their savings is taxed at the starting rate of 0%. It is important to note that this situation is rare. If an individual has NSNDI that exceeds £5,3000 up to £37,700 then interest on those savings is taxed at the basic rate of 20% and if their taxable income exceeds £37,701, then the interest on their savings will be taxed at the higher rate of 40%.

**SLIDE 6 – RATES OF TAX - DIVIDENDS**

When taxing an individual’s income from dividends these dividends are taxed at 8.75% for basic rate, 33.75% for higher rate and 39.35% for additional rate taxpayers.

**SLIDE 7 – ORDER OF TAXATION**

How do these rates fit in to the income tax calculation? You will recall from listening to the online lectures to calculate an individual’s tax liability there are 5 stages that need to be worked through. Once you have calculated an individual’s total income, the net income and taxable income, you then need to split that taxable income into its different sources and tax these sources at the appropriate rate. You then must remember to tax the sources in the appropriate order. So first you will tax the NSNDI, then you will tax the income from savings and then you will tax the income from dividends.

**SLIDE 8 – SEPARATE TYPES OF INCOME**

Let’s see how this works by looking at a basic calculation. Let’s say that A has taxable income of £90,000. Before we can tax the income at the appropriate rate, we need to separate it into sources of income. Of that £90,000, £82,000 is NSNDI and that is taxed first. We got to the figure of £82,000 by deducting the savings income of £2,000 and the dividend income of £6,000. Next, we would tax the £2,000 income from savings and then the £6,000 dividend income.

**SLIDE 9 – TAXING NSNDI**

You will recall me mentioning that when we tax each type of income, we must use each band in its entirety before moving on to the next. You can see an example on the screen of how this works.

**SLIDE 10 TAXING SAVINGS**

You also need to know about the personal savings allowance in relation to income on savings. When taxing interest on savings, if an individual is a basic rate income taxpayer the first £1000 of their interest on savings is tax free, If an individual is a higher rate tax payer they receive a personal savings allowance of £500. Unfortunately, additional rate taxpayers do not receive any personal savings allowance.

**SLIDE 11 – TAXING SAVINGS**

Let’s have a look at an example.

If A had an income from running a business of £25,000 and also received interest on savings of £800, how much tax would he pay on his savings? Pause the audio lecture now and have a go at working out the calculation.

How did you get on? Hopefully, you have worked out that A does not pay any tax on his savings. You have been told that A has an income from running a business of £25,000 and this makes him a basic rate taxpayer and therefore the first £1,000 of interest on his savings is tax free.

Let’s have a look at another calculation.

If A had an income from running a business of £50,000 and also received interest on savings of £1,000, how much tax would he pay on his savings here?

Pause the audio lecture whilst you work out the calculation.

How did you get on? Hopefully, you have an answer of £200. Here you can see that A is a higher rate income taxpayer. As a higher rate income taxpayer, he receives a personal savings allowance of £500. The remaining £500 is taxed at the higher rate of 40% so he has £200 of income tax to pay.

 **SLIDE 12 – TAXING DIVIDENDS**

You also need to know about the dividend allowance and this works in a similar way to the savings allowance. The dividend allowance is £2000 for all individuals whether they are a basic, higher or an additional rate taxpayer. So, everyone has a £2000 dividend allowance.

If an individual receives more than £2,000 dividend income, this is taxed at the appropriate rate depending on whether they are a basic, higher or additional rate taxpayer.

**SLIDE 13 – TAXING DIVIDENDS**

Let’s have a look at an example.

If A had an income from running a business of £80,000 and also received dividends of £1,500, how much tax would he pay on his dividends?

Pause the audio lecture whilst you work out the calculation.

How did you get on? Hopefully, you have worked out that A does not pay any tax on these dividends. As you know A receives a dividend allowance of £2,000. The £1,500 dividend he receives is covered by his £2,000 dividend allowance.

In the next example, A had an income from running a business of £50,000 and also received dividends of £10,000. Take a moment here to work out how much tax he would have to pay on his dividends, pausing the audio lecture while you do so.

How did you get on? Hopefully, you will have an answer of £2,700. As you can see A is a higher rate taxpayer and he has a £2,000 dividend allowance. This leaves him with £8,000 which will have to be taxed at the higher rate of 33.75% and so the tax bill here is £2,700.

**SLIDE 14 – PAYMENT OF TAX**

Lastly, let’s talk about when the income tax liability has to be paid. First of all, it’s important to note that the tax year isn’t the same as our calendar year. The tax year runs from 6 April to the following 5 April. Tax is either paid because it’s deducted at source, or by self-assessment by completing an annual tax return. Most people get paid their salary and income tax is deducted at source under PAYE – pay as you earn. An example of where you might use self-assessment is where you are, or you represent an individual who is self-employed.

For individual’s using the self-assessment method to pay their income tax, they make three payments to HMRC. Two payments are made on account based on an estimate of what tax is owed to the revenue and the third is to pay the balance.

You can also see on the slides the dates when tax is paid using the self-assessment method.