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WEALTH **KNOWLEDGE**

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In this month's Wealth Knowledge...A new personal savings allowance will allow individuals to earn up to £1,000 a year in interest tax-free. The 10% dividend tax credit has been replaced by a £5,000 annual allowance. The eligibility criteria for the new state pension could mean that thousands of people are not eligible for the full amount. And, the chancellor announced details of a new lifetime ISA in his Budget 2016 speech.

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Personal savings allowance confuses savers

90% of savers are still unsure what the personal savings allowance (PSA) is and are struggling to decide what to do with their savings income, according to research by AA Financial.

Basic rate taxpayers can earn up to £1,000 of savings income tax-free, while those paying the higher rate will be able to earn up to £500 tax-free.

Savings income that applies under the allowance can range from interest from bank and building society accounts, interest distributions from unit trusts and annuity payments.

The following tax rates will apply with the new allowance based on your adjusted net income:

- basic rate (20%) – £1,000 tax-free savings allowance
- higher rate (40%) – £500 tax-free savings allowance
- additional (45%) – no PSA.

PSA considerations

The PSA can seem complex to some who are new to savings and looking to protect their income. Here are 4 important points to consider when coming up with a savings strategy:

- interest rates can affect whether you'll exceed your allowance
- a pay rise can affect the value of your PSA
- interest from ISAs remains tax-free and does not count towards your PSA
- spouses can inherit ISA allowances from a deceased partner.

HMRC will be responsible for collecting tax by changing your tax code if your savings income exceeds £1,000.

Get in touch to talk about the PSA.

Dividend taxation changes for 2016/17

The system of dividend taxation has undergone major changes for the 2016/17 tax year.

In a bid to simplify the rules, the 10% tax credit has been abolished and an annual dividend tax allowance of £5,000 has been introduced.

Dividend income exceeding the £5,000 allowance and the personal allowance for income tax will be taxed at the following rates:

- basic rate: 7.5%
- higher rate: 32.5%
- additional rate: 38.1%.

Dividend income that is within the £5,000 allowance will be tax-free. Any unused personal allowance can also be used against dividend income.

The government estimates that over 75% of people who receive dividend income will either gain or be unaffected by these changes.

A further 1 million individuals will see a tax reduction on their dividend income.

Points to consider

Although the new rules are simpler than the previous regime, there are still some important details to be aware of:

- the £5,000 allowance will not reduce total income for tax purposes and will only apply to dividend income
- dividends paid within pension funds and those received on shares from ISAs will stay tax-free
- no tax will be deducted at source; it will be paid through self-assessment
- the £1,000 personal savings allowance (£500 for higher rate taxpayers) excludes dividend income.

How the changes affect your tax planning will depend on your individual circumstances and any other sources of income.

We can explain how changes to dividends will affect you.

New state pension: do you qualify?

The rules for qualifying for the new state pension may mean that some people set to retire in the next 15 years miss out.

The new system requires that individuals have a minimum of 10 qualifying years of national insurance contributions (NICs) in order to be eligible. To receive the full amount, an individual will need 35 qualifying years.

Age UK has estimated that this could mean that around 50,000 women and 20,000 men may not qualify for the full state pension.

Caroline Abrahams, charity director at Age UK, said:

"The reality is that the news will be good for some but disappointing for others, which is why it is so important for everyone approaching retirement to check their state pension age and what they'll receive when they reach it."

Increasing your state pension

Anyone reaching state pension age on or after 6 April 2016 will be covered under the new system.

The full amount that a person can receive in 2016/17 is £155.65.

Your national insurance record will be used to determine the starting amount you will receive. If you do not think that this will be adequate there are a number of ways that this amount can be potentially increased:

- make additional NICs
- claim national insurance credits
- delay starting your state pension
- make voluntary contributions to fill any gaps in your NICs record.

Contact us to talk about your retirement today.

Lifetime ISA introduced

The new lifetime ISA announced by George Osborne in Budget 2016 will bring additional flexibility for younger people, according to Standard Life.

From April 2017, adults aged under 40 can save a maximum of £4,000 a year and receive a 25% government bonus. The money can be used to purchase your first home, or be kept until you're 60 to be used to fund retirement.

The annual ISA allowance will also be increased from April 2017 from £15,240 to £20,000.

In his Budget speech, Chancellor George Osborne said:

"For the basic rate taxpayer, that is the equivalent of tax-free savings into a pension, and unlike a pension you won't pay tax when you come to take your money out in retirement."

Saving for your first home or for retirement

The government hopes that the lifetime ISA will provide a boost to those who are looking to purchase their first home or saving for retirement.

First-time buyers can use their savings as a deposit on their first home worth up to £450,000.

Those with a Help to Buy ISA can transfer savings into the lifetime ISA from April 2017, or continue to use both accounts but can only use 1 bonus to buy a home.

People saving for retirement can withdraw money at any time before the age of 60. However, a 5% charge will be incurred and they will lose the government bonus and any interest or growth earned on the bonus.

Contact us today to discuss your savings.