

## Finance Bill 2025-26

### Clause 10 – Basic rate limit and personal allowance for tax years 2028-29 to 2030-31 Briefing from the Low Incomes Tax Reform Group (LITRG)

#### 1 Executive Summary

- 1.1 Clause 10 extends the freeze of the personal allowance and basic rate income tax band for a further three tax years until 2030/31.
- 1.2 We are concerned about the impact of the freeze on people with low incomes who are paying a larger share of their income in tax, meaning that they face a real reduction in their net disposable income.
- 1.3 An increasing number of people are being brought into income tax and therefore having to deal with the administrative complexities of the tax system. This also places an additional burden on HMRC's resources. Additional funding should be provided to ensure HMRC can meet these extra demands.
- 1.4 Although not included in this bill, the government has also announced its intention to ease the administrative burden for certain recipients of the state pension affected by the continued freeze of the personal allowance threshold, and the Chancellor has since confirmed that small tax liabilities owed by these people will not be collected. We welcome measures that simplify administration but urgently request clarification of the scope of this proposal, which now appears to extend beyond an administrative easement<sup>1</sup>.

#### 2 Impact of Clause 10

- 2.1 The following amounts are to be frozen until 5 April 2031, by which time they will have remained unchanged for 10 years:
  - Personal allowance – £12,570, and
  - Basic rate limit – £37,700 (i.e. most people will start to pay the higher rate of tax once income exceeds £50,270<sup>2</sup>).

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<sup>1</sup> See LITRG blog December 2025 "The state pension tax debate – issues arising from the budget 2025 announcement": <https://www.litrg.org.uk/blog-post/state-pension-tax-debate-issues-arising-budget-2025-announcement>

<sup>2</sup> Those who are entitled to the blind person's allowance will have a higher threshold for the higher rate of tax.

2.1.1 According to the Office for Budget Responsibility (OBR)<sup>3</sup>, if the personal allowance and basic rate tax limit had been uprated in line with inflation since they were set at these amounts in 2021/22, by 2030/31 they would be £17,470 and £57,800 respectively.

## 2.2 General impact

2.2.1 Freezing the personal allowance and the basic rate tax limit increases tax liabilities but in an arguably less transparent way than changing headline tax rates. It causes their value to erode over time due to inflation. As a result of this ‘fiscal drag’, people become taxpayers for the first time or move into higher tax bands even if their incomes have only increased in line with inflation and do not represent any real increase in purchasing power.

2.2.2 The freeze on income tax thresholds was previously due to end in April 2028. The OBR has said that the extension of the freeze for a further three years to April 2031 will mean 780,000 more people being brought into paying income tax and 920,000 more paying tax at the higher rate<sup>4</sup>.

2.2.3 In Budget 2024 the government committed to increasing HMRC’s resources as part of its package to close the ‘tax gap’<sup>5</sup>. However, as more people are brought into the tax net as a result of the freeze to the thresholds applied by clause 10, there is likely to be an increased strain on HMRC’s day to day customer service. Additional funding will be required to ensure HMRC can adequately support the higher numbers of taxpayers, especially those who find themselves having to navigate the tax system for the first time, or those with complex tax affairs. No reference to these additional costs was made in the 2025 budget documents.

## 2.3 Impacts on those with low incomes

2.3.1 Individuals with low incomes are disproportionately impacted by the freezing of income tax thresholds as they suffer the largest reduction in their net income in real terms<sup>6</sup>.

2.3.2 Those on low incomes may be least able to deal with the tax system’s administrative complexity. They may face unexpected liabilities and come across unfamiliar systems and documents, requiring extra support. For example:

- Someone moving into the PAYE system may find they have to try to understand a PAYE coding notice for the first time;
- Some individuals may find it difficult to budget during the tax year if their net pay or pension is lower than expected because tax starts to be deducted at source;

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<sup>3</sup> [CP 1439 – Office for Budget Responsibility – Economic and fiscal outlook – November 2025](#) box 3.3

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<sup>5</sup> Budget 2024, paragraph 2.16 [Autumn Budget 2024 print](#)

<sup>6</sup> An individual whose income of £15,000 in tax year 2025/26 increases to £17,400 in 2030/31 (approx. 3% increase p.a.) will see their tax liability increase from £486 to £966. This represents an increase in the effective tax rate suffered of 2.3%. In contrast, someone whose income increases at the same rate over the same period from £40,000 to £46,400 will see an increase of 0.9% in their effective rate of tax (liabilities of £34,514 and £39,634 respectively).

- Someone moving into the simple assessment system may receive a simple assessment tax bill a few months after the end of the tax year and not have budgeted for the tax liability.

- 2.3.3 Pay increases linked to minimum wage uprating or inflation are increasingly taxed, thereby reducing their value in real terms. To illustrate, workers earning the minimum wage who work only 20 hours per week already pay some income tax on their earnings<sup>7</sup>.
- 2.3.4 Workers with plan 2 student loans<sup>8</sup> face an additional real tax increase as the plan 2 repayment threshold is frozen until 2029/30<sup>9</sup>.
- 2.3.5 Where individuals claim universal credit, the impact of paying income tax, or more income tax, is mitigated to some extent as universal credit uses the net earnings figure and, therefore, rises as net earnings is reduced due to tax. However, universal credit does not mitigate the reduction in net earnings pound for pound<sup>10</sup>.

## 2.4 Additional impacts on state pensioners

- 2.4.1 The full new state pension is set to exceed the personal allowance from April 2027 and will continue to increase in subsequent years as a result of the triple lock guarantee<sup>11</sup>, bringing more state pensioners into the tax net<sup>12</sup>.
- 2.4.2 The state pension is taxable income, but tax is not withheld at source. HMRC rely on post-year tax collection mechanisms (simple assessment, self assessment) and PAYE coding adjustments to collect any tax due, which can result in confusion and cashflow difficulties for pensioners. These issues are likely to become more widespread.
- 2.4.3 Our concerns about the methods and timing of collection of tax due on the state pension and the risk of unexpected tax bills for pensioners were expressed in our 2025 Budget submission in which we recommended bringing the state pension into its own system of PAYE<sup>13</sup>.

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<sup>7</sup> The national living wage is £12.21 per hour from April 2025. Currently, working 20 hours per week, 52 weeks per year, produces gross earnings of £12,698, which exceeds the personal allowance of £12,570. The NLW will increase to £12.71 from April 2026.

<sup>8</sup> GOV.UK sets out the different types of repayment plans for student loans at <https://www.gov.uk/repaying-your-student-loan/which-repayment-plan-you-are-on>.

<sup>9</sup> Budget 2025, paragraph 4.113 [HC 1492 – Budget 2025 Strong Foundations, Secure Future – November 2025](#)

<sup>10</sup> The maximum amount of a universal credit award is reduced using a taper rate of 55% of net earnings, although earnings below the work allowance are ignored.

<sup>11</sup> The full new state pension in 2026/27 will be £12,548. The minimum inflationary increase under the triple lock of 2.5% would result in the full new state pension exceeding the personal allowance from 2027/28.

<sup>12</sup> HM Revenue & Customs [Number of individual Income Tax payers](#) 25 June 2025: The number of people of state pension age paying income tax is projected to increase from 6.47million in tax year 2020/21 (being the final year before the freeze on the personal allowance was applied) to 8.72million in 2025/26. This taxpayer number is expected to increase sharply in the coming years as a result of the frozen personal allowance and the triple lock.

<sup>13</sup> See LITRG budget 2025 submission “Bringing the state pension into PAYE”: <https://www.litrg.org.uk/submissions/2025-autumn-budget-submission-litrg-recommends-bringing-state-pension-pay>

### **3 Easing the administrative burden for pensioners**

- 3.1 The Budget document states that the government will seek to ease the administrative burden of simple assessment for pensioners whose only income is the basic or full new state pension without increments<sup>14</sup>.
- 3.2 The Chancellor has since gone further and confirmed that the tax burden will be removed entirely for these pensioners, saying that their small tax liabilities will not be payable “in this parliament”<sup>15</sup>.
- 3.3 The proposal to waive tax liabilities payable by only certain taxpayers raises questions of fairness across the pensioner population and indeed across the wider population of taxpayers<sup>16</sup>. Taxpayers with a similar level of total gross income may face different tax treatment and find themselves worse off simply because their income comes from different sources, rather than all being from state pension.
- 3.4 For example, pensioners who don’t qualify for the easement but have total income at a similar level as someone receiving the full new state pension, perhaps from a smaller state pension entitlement and an additional small private pension, will have lower net income because of the income tax charge suffered.
- 3.5 Some pensioners already have state pension income higher than the personal allowance as a result of increments. In some cases, the state pension can be as much as £20,000 a year. The suggestion appears to be that these people will not benefit from the proposed easement.
- 3.6 This state pension tax easement raises a number of questions, for which urgent clarification is required:
- Will the easement operate via HMRC discretionary care and management powers, or will there be formal legislation?
  - What will the precise eligibility criteria be? Will state pensioners be able to be in receipt of any other kind of income, enhanced state pension or state benefits and remain eligible for the relief?
  - In practical terms, how will HMRC identify eligible state pensioners, in the absence of requiring declarations and/or evidence?
  - As it appears that the Exchequer will be forgoing tax receipts, what are the costs related to this announcement? (None were included in the Budget document.)
- 3.7 There is no operational detail available currently. We would welcome a government consultation on this proposal. This could consider how it fits with the wider tax system and alternative approaches that would both meet the government’s objectives and create a better long-term solution if

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<sup>14</sup> Budget 2025, paragraph 4.167 [HC 1492 – Budget 2025 Strong Foundations, Secure Future – November 2025](#)

<sup>15</sup> For example, see: [The Chancellor confirms those who only get State Pension WON'T pay income tax on it this Parliament](#) (Moneysavingexpert.com, 28 November 2025).

<sup>16</sup> See LITRG blog – Potential Inequalities - [The state pension tax debate – issues arising from the budget 2025 announcement | Low Incomes Tax Reform Group](#)

allowances are to remain frozen. For example, arguably simpler and more transparent options would be to increase the personal allowance in line with the full new state pension, to reintroduce age-related personal allowances, or to bring the state pension within the PAYE system.

#### **4 About Us**

- 4.1 The Low Incomes Tax Reform Group (LITRG) is an initiative of the Chartered Institute of Taxation (CIOT) to give a voice to the unrepresented. Since 1998, LITRG has been working to improve the policy and processes of the tax, tax credits and associated welfare systems for the benefit of those who are least able to pay for professional advice. We also produce free information, primarily via our website, to help make a difference to people’s understanding of the tax system.
- 4.2 LITRG works extensively with key stakeholders such as HM Revenue & Customs (HMRC) and other government departments, commenting on proposals and putting forward our own ideas for improving the tax system. LITRG also considers the welfare benefits system, and other related systems, to the extent that they interact with tax.
- 4.3 The CIOT is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT’s primary purpose is to promote education and study of the administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.

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