Dividend allowance and dividend nil rate; abolition of dividend tax credits, etc.
Consultation on draft clauses for Finance Bill 2016
Response from the Low Incomes Tax Reform Group (LITRG)

1 Executive Summary

1.1 We welcome the opportunity to comment on the draft legislation to introduce a new dividend allowance and dividend nil rate for the first £5,000 of an individual's dividend income and to abolish the dividend tax credit.[1]

1.2 We note that for individuals with modest amounts of dividend income, this legislation is likely to simplify their position. However, as we have previously pointed out, there will be additional complexity for some.[2] In particular, some individuals will find themselves within self assessment for the first time as a direct result of the changes and this will likely be an unwelcome burden in time and cost. In addition, some individuals who make donations under Gift Aid may find themselves with an unexpected tax bill, if they are used to relying on the dividend tax credit to cover the Gift Aid relief.[3]

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[1] Draft clauses 2 and 3 of Finance Bill 2016.

[2] http://www.litrg.org.uk/latest-news/news/150709-mixed-bag-summer-budget-%E2%80%93-many-low-income-workers-lose-out; http://www.litrg.org.uk/latest-news/news/150708-tax-charity-extends-qualified-welcome-tax-free-dividend-allowance-litrg

[3] http://www.litrg.org.uk/latest-news/news/151027-tax-charity-criticises-hmrc-targeting-compassionate-individuals-rather

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1.3 We therefore call on HM Revenue & Customs (HMRC) to ensure that clear guidance is made available and also that there is good, pro-active publicity and communications to draw people's attention to the changes. This will help to ensure that taxpayers better understand what the changes mean for them and also enable taxpayers to reorganise their affairs in good time, if appropriate.

2 About Us

2.1 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 on low incomes. Everything we do is aimed at improving the tax and benefits experience of low income workers, pensioners, migrants, students, disabled people and carers.

2.2 LITRG works extensively with HMRC and other government departments, commenting on proposals and putting forward our own ideas for improving the system. Too often the tax and related welfare laws and administrative systems are not designed with the low-income user in mind and this often makes life difficult for those we try to help.

2.3 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.

3 General comments

3.1 While we broadly welcome the introduction of the £5,000 dividend allowance, as this will offer simplification for many recipients of dividend income, we note that some people on overall modest incomes may now have to start paying tax on their dividend income if it exceeds £5,000; in addition, they may also have to start submitting self assessment tax returns.[4] According to the policy paper published alongside the draft legislation, approximately 200,000 extra individuals are expected to have to pay tax on their dividend income as a result of the reforms. Of these, approximately 8,500 individuals are likely to have to tell HMRC about their dividend income for the first time, and have to enter self

[4] http://www.litrg.org.uk/latest-news/news/150708-tax-charity-extends-qualified-welcome-tax-free-dividend-allowance-litrg

assessment.[5] This means that good, proactive communications will be critical to the successful operation of the dividend allowance.

3.2 It appears that the dividend allowance and dividend nil rate will not be available to personal representatives or executors of estates in administration. Currently, HMRC do not require the completion of a tax return for certain estates in administration – the main criterion being that the tax liability must not exceed £10,000.[6] The abolition of the 10% dividend tax credit may result in some personal representatives facing an increased compliance burden, for example where the 10% dividend tax credit previously satisfied all the tax liability in respect of dividend income. Together, the ending of the deduction of tax at source from interest and the abolition of the dividend tax credit may mean there is an argument for considering an increase in the figure for informal settlement, with a view to minimising compliance costs for estates with small tax liabilities.

3.3 It is notable that the dividend allowance does not operate as a typical allowance. It is a nil rate band of tax that does not extend the basic or higher rate bands. Although the operation of the allowance is not conceptually confusing in itself, it would be more transparent and simpler to term it a zero tax band rather than describing it misleadingly as an allowance.

3.4 Given the points made above, we recommend that HMRC ensure their guidance is clear, and that there is a good, pro-active communications strategy to ensure that taxpayers are fully aware of the changes, how they affect them and what action they need to take to ensure they comply. We recommend that HMRC also undertake an analysis to ensure that they understand which groups of taxpayers are affected and how best to contact them. In particular, we are concerned that some of those affected will be pensioners for whom digital forms of communication may not be suitable.

4 Comments on draft legislation

4.1 *Dividend allowance and dividend nil rate*

4.1.1 We have no comments on the draft legislation.

4.1.2 We note however that the new dividend rates of tax (7.5%, 32.5% and 38.1%) are not included in draft clause 2 of Finance Bill 2016. We would expect these to appear in the rate-setting parts of Finance Bill 2016 in due course.

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[5] https://www.gov.uk/government/publications/income-tax-changes-to-dividend-taxation/income-tax-changes-to-dividend-taxation#detailed-proposal

[6] http://www.hmrc.gov.uk/manuals/tsemmanual/tsem7410.htm

4.2 ***Abolition of dividend tax credits etc.***

4.2.1 We have no comments on the draft legislation.

LITRG
26 January 2015