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The impact of the Social Care Levy

on your clients

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[Technical Eye]

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From 6 April 2022, new measures to fund adult social care will give rise to a 1.25 percentage points increase in both National Insurance Contributions and the rate of income tax payable on dividends (see our article Funding adult social care: has the problem been solved?). Here we discuss the impact this Levy might have on your clients.

The impact on National Insurance Contributions (NIC)

Initially, the increase in NIC will be collected via the current mechanism under PAYE or Self-Assessment, then from April 2023 it will be treated as an entirely separate form of tax, referred to as the **Health and Social Care Levy** (HSCL).

This will be ringfenced for use only in relation to health and social care and as an addition to the existing NHS allocation. To put this increase in NICs into context, here is an example of the difference it could make.

The separation of the HSCL from mainstream NIC from 6 April 2023 will enable the government to widen the scope of the provisions to bring in post state pension age workers who are currently out of scope of the Class 1 employee and Class 4 NIC rules.

So, from 2023/24 onwards:

+ Self-employed individuals over state pension age will pay the HSCL at 1.25% on profits exceeding the NIC threshold of £9,568.
+ Employees over state pension age will pay HSCL at 1.25% on earnings above the threshold of £9,568 (employers already pay secondary NIC on earnings above £8,840 but the rate will also increase by 1.25%).

Julian, age 52, self-employed with a profit of £100,000

As the table below shows, Julian can expect an increase in NIC of £1,130.40, which effectively represents nearly a 24% increase in real terms.

Class 4 NIC	Threshold		2021/22		2022/23
		Rate	£	Rate	£
Profit	100,000				
Lower threshold	9,568	0%	0		0
Upper threshold 50,270 - 9,568	40,702	9%	3,663.18	10.25%	4,171.96
Excess	49,730	2%	994.60	3.25%	1,616.23
Total due			**4,657.78**		**5,788.18**

If Julian had been over state pension age in the current 2021-22 tax year, the calculation would be somewhat different, as the implementation of the increased rate for people over state pension age has been delayed until 6 April 2023:

Class 4 NIC	Threshold	2021/22		2021/23		2022/24	
		Rate	£	Rate	£	Rate	£
Profit	100,000						
Lower threshold	9,568	0%	0		0	0	
Upper threshold 100,000 - 9,568	40,702	0%	0.00	0%	0.00	1.25%	1,130.40
Total due				**4,657.78**			**1,130.40**

As both Class 2 and 3 NIC are not linked to profit but are a flat monetary amount payable on a weekly basis, the 1.25% increase won't apply.

+ Summary of changes

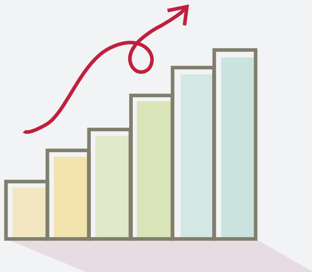
- Class 1 & 4 NICS are increasing by 1.25% for people under state pension age with effect from 6 April 2022
- The increase in rate will also apply to people over state pension age from 6 April 2023
- The increase will not apply to Class 2 or 3 NIC
- The rate of income tax payable on dividends will also increase from 6 April 2022:
  - Basic rate increases to 8.75%
  - Higher rate increases to 33.75%
  - Additional rate increases to 39.35%
- Trustee's standard rate is increased to 8.75% and the trust rate is increased to 39.35%
- ISAs are outside of the scope of the new dividend tax rate
- Single premium investment bonds are not affected by the increase in dividend tax rate

The impact on dividend income tax rate

The rate of income tax payable on dividend income will increase by 1.25 percentage points from 6 April 2022, although the dividend allowance of £2,000 will remain in place.

The new rates will be:

- Basic rate increased to 8.75% from 7.5%
- Higher rate increased to 33.75% from 32.50%
- Additional rate increased to 39.35% from 38.1%



Once again, the funds raised from the measure will be ringfenced to contribute towards the health and social care budget, along with the HSCL. For clients affected by this increase, along with the effect of the HSCL, the impact will be noticeable as the following example shows:

Julian, age 52, private company director taking a salary of £12,570 and dividend of £37,700 with no Benefits in Kind

Class 1 NIC	Threshold	2021/22		2022/23	
		Rate	£	Rate	£
Salary	12,570				
Primary Rate - employee					
Lower threshold	9,568	0%	0	0%	0
Excess	3,002	12%	360.24	13.25%	397.77
Secondary Rate - employer					
Lower threshold	8,840	0%			
Excess	3,730	13.8%	514.74	15.05%	561.37
Tax on Dividend					
Total Dividend £37,700					
Less Allowance 2,000	35,700	7.5%	2,677.50	8.75%	3,123.75
Total due			**3,552.48**		**4,082.88**

N.B. Dividend income arising within an ISA is sheltered from this increase as an ISA is already exempt from income and capital gains tax (CGT).

Impact on trustees

The new highest tax rate for dividends for trustees (where the trust income is subject to tax in the trustee's hands) will be 39.35%, with effect from 6 April 2022.

While trustees cannot benefit from the £2,000 dividend allowance, they are entitled to claim a £1,000 standard rate band against income. This can be divided depending on the number of trusts a settlor has created (up to a maximum of five), meaning that a proportion of dividend income may only be taxable at 8.75% in future, with the balance being taxed at the full rate of 39.35%.

However, given that income distributions to beneficiaries will continue to be franked with a refundable tax credit of 45%, the increase in rate payable by the trustees can still be reclaimed by a non-tax paying beneficiary, provided the trustee's income distribution policy is carefully managed.

That said, trustees who invest in investment bonds, whether onshore or offshore, can benefit from the same dividend income stream held within the underlying funds of the bond without immediate exposure to income tax or CGT.

Conclusion

If investments within a trust are subject to dividend tax, provided the terms of the trust do not specify for natural income to be provided to a life tenant and it allows the trustees to have wide powers of investment, a re-structure of the investments to purchase an investment bond might be worth consideration by the trustees, subject to any CGT implications on the sale of directly held investments.

Given that investment bonds are non-income producing assets, it would also reduce the ongoing tax reporting requirements to HMRC under the chargeable event regime. But trustees would only need to complete a trustee tax return upon a chargeable event, so it's important they're aware of how an investment bond will be taxed when held within a trust.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Legal disclaimer

This document is based on Canada Life's understanding of applicable UK tax legislation and current HM Revenue & Custom's practice, as at March 2022 and could be subject to change in the future.

It is provided for professional advisers only. Any recommendations are the adviser's sole responsibility.

For more information, please contact our technical team at **ican@canadalife.co.uk**

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