

## **Research Note:**

# **Consequences of the freeze in the income tax personal allowance on State Pension amounts**

October 2024

## Introduction

In 2010, the then Government announced the introduction of the State Pension triple lock, meaning that the State Pension would increase each April by the highest of inflation<sup>1</sup>, average earnings<sup>2</sup> or 2.5%. The current Government announced in their manifesto<sup>3</sup> that they “*will retain the triple lock for state pension*” and it is therefore expected that the State Pension will rise by the highest of inflation, average earning or 2.5% each April until the next General Election.

In 2021, the then Chancellor of the Exchequer announced in his Budget 2021 speech<sup>4</sup> that “*income tax personal allowance...[will] increase...next year to £12,570, but we will then keep it at this more generous level until April 2026.*” Less than two years later his successor but one announced in his Autumn Statement 2022 speech<sup>5</sup> that “*I am maintaining at current levels the income tax personal allowance...for a further two years taking us to April 2028.*” And then in 2024, the Chancellor of the newly elected Government, announced in her Autumn Budget 2024 “*The government will not extend the freeze to income tax...From April 2028... will be uprated in line with inflation*<sup>6</sup>”.

The freezing of the income tax personal allowance, alongside the State Pension increasing in line with the triple lock, will lead to some pensioners receiving a State Pension amount that is above the income tax personal allowance. In this note we present when the full rate of the basic and the new of State Pension will rise above the income tax personal allowance, and an estimate of the number of pensioners who will receive a State Pension amount that is subject to income tax. We will then conclude with a discussion. Annex A presents the methodology behind our estimates.

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<sup>1</sup> Inflation is measured by the rate of the Consumer Price Index in the September of the previous year

<sup>2</sup> Average earnings are defined as increase in total UK wages for May to July of the previous year

<sup>3</sup> Labour. *Change. Labour Party Manifesto 2024* [online Available at <https://labour.org.uk/wp-content/uploads/2024/06/Change-Labour-Party-Manifesto-2024-large-print.pdf> [Accessed 24<sup>th</sup> October 2024]

<sup>4</sup> HM Treasury. 3<sup>rd</sup> March 2021. *The Budget 2021 speech as delivered by Chancellor Rishi Sunak.* [online] available at <https://www.gov.uk/government/speeches/budget-speech-2021#:~:text=Our%20borrowing%20is%20the%20highest,livelihoods%20of%20the%20British%20people.> [Accessed 24<sup>th</sup> October 2024]

<sup>5</sup> HM Treasury. 17<sup>th</sup> November 2022. *The Autumn Statement 2022 speech as delivered by Chancellor Jeremy Hunt.* [online] Available at <https://www.gov.uk/government/speeches/the-autumn-statement-2022-speech#:~:text=We%20have%20to%20take%20difficult,set%20out%20in%20cash%20terms.> [Accessed 24<sup>th</sup> October 2024]

<sup>6</sup> HM Treasury. 30<sup>th</sup> October 2024. *Autumn Budget 2024. Fixing the Foundations To Deliver Change.* [online] Available at <https://www.gov.uk/government/publications/autumn-budget-2024> [Accessed 30<sup>th</sup> October 2024]

## Basic State Pension

In the UK if you are a man born before 6th April 1951 or a woman born before 6th April 1953, you will get the **basic** State Pension. Pensioners in receipt of the basic State Pension can get up to £169.50 per week in 2024-25. The amount of the basic State Pension that any one pensioner will receive will depend on their number of qualifying years of National Insurance. In some instances, a pensioner may receive more than this weekly amount if they are eligible for Additional State Pension, or they delayed (deferred) taking up their State Pension. The triple lock does not apply to the Additional State Pension, or any additional amount received by having deferred take up of the State Pension<sup>7</sup>.

The State Pension triple lock means that the basic and new State Pension will increase in April 2025 by average earnings (4.1%) since this was higher than inflation (1.7%) and the 2.5% figure<sup>8</sup>. Table 1 shows the full rate of the **basic** State Pension by the end of 2029-30 (assuming the State Pension rises by 2.6% in 2026-27 and then 2.5% for each subsequent year<sup>9</sup>).

Table 1: Annual amounts of basic rate of basic State Pension

	2024-25	2025-26	2026-27	2027-28	2028-29	2029-30
Annual amounts	£8,814.00	£9,175.37	£9,413.93	£9,649.28	£9,890.51	£10,137.78

Source: Author's calculations using on Department for Work & Pensions (DWP) data

Table 1 shows that by the end of 2029-30, pensioners on the full rate of the **basic** State Pension will be entitled to an annual amount below the income tax personal allowance. However, that does not mean that no pensioners will be paying income tax on their **basic** State Pension, because some, entitled to an amount higher than the full rate<sup>10</sup> may be receiving an amount that is above the income tax personal allowance.

<sup>7</sup> The Government can however choose to increase these amounts by the triple lock

<sup>8</sup> The Government is legally required to increase the State Pension each year at least in line with average earnings. If average earnings are below the rate of inflation or 2.5%, it is for the Government to proactively decide if it wishes to increase the State Pension above the rate of average earnings.

<sup>9</sup> The decision by the current Government to commit to the triple lock means, based on the Office for Budget Responsibility (OBR) forecasts, the State Pension will rise by 2.6% in April 2026 and then by 2.5% in April 2027 and each subsequent year until the General Election.

<sup>10</sup> Because they are entitled to an Additional State Pension and/or are in receipt of a delayed (deferred) State Pension

Table 2 shows the proportion of pensioners in receipt of the **basic** state pension whose amount received is higher than the income tax personal allowance. This may be because in addition to the rate of the basic State Pension they are entitled to an Additional State Pension and/or are in receipt of a delayed (deferred) State Pension. The figures are presented for the three years 2021-22<sup>11</sup>, 2024-25 and 2029-30<sup>12</sup>.

Table 2: Proportion and number of pensioners in receipt of the basic state pension whose amounts received are higher than the income tax personal allowance

	2021-22	2024-25	2029-30
Proportion	5%	13%	39%
Number	0.5 million	1.2 million	3.6 million

Source: Author’s calculations using on Department for Work & Pensions (DWP) data

Table 2 shows:

- in 2021-22, when the income tax personal allowance was raised to £12,570, around one in twenty (5%) pensioners in receipt of the **basic** State Pension received an amount that was above the income tax pension allowance. This equated to around half a million such pensioners.
- in 2024-25 (today), with the income tax personal allowance having been kept that the same level, around one in seven (14%) pensioners in receipt of the **basic** State Pension are receiving an amount that is above the income tax pension allowance. This equates to around 1.2 million such pensioners; an increase of around 0.7 million such pensioners since the allowance has been kept at the same level.
- in 2029-30, the last possible year in which the next General Election can be held, around two in five (39%) pensioners in receipt of the **basic** State Pension are estimated to receive an amount that is above the income tax pension allowance. This equates to around at least 3.6 million such pensioners; an increase of at least 2.4 million such pensioners from today and at least 3.1 million such pensioners since the allowance has been kept at the same level.

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<sup>11</sup> The year the income tax personal allowance was raised to £12,570

<sup>12</sup> The last year in which the next General Election can be held

## New State Pension

In 2016, the then Government introduced changes to the State Pension system, meaning that if you are a man born before 6th April 1951 or a woman born before 6th April 1953, you will get the **new** State Pension.

Pensioners in receipt of the **new** State Pension can get up to £221.21 per week in 2024-25. The amount of the new State Pension that any one pensioner will receive will depend on their number of qualifying years of National Insurance. In some instances, a pensioner may receive more than this weekly amount if they delayed (deferred) taking up their State Pension and/or have protected payments from the previous system.

The State Pension triple lock means that the basic and new State Pension will increase in April 2025 by average earnings (4.1%) since this was higher than inflation (1.7%) and the 2.5% figure<sup>8</sup>. Table 3 shows the full rate of the **new** State Pension by the end of 2029-30 (assuming the State Pension rises by 2.6% in 2026-27 and then 2.5% for each subsequent year<sup>9</sup>).

Table 3: Annual amounts of new rate of basic and new State Pension

	2024-25	2025-26	2026-27	2027-28	2028-29	2029-30
New State Pension	£11,502.92	£11,974.54	£12,285.88	£12,593.02	£12,907.85	£13,230.55
Income tax liable	N/A	N/A	N/A	£4.60	£14.78	£25.41.53
Take home amount	£11,502.92	£11,974.54	£12,285.88	£12,588.42	£12,893.07	£13,205.13

Source: Author's calculations using on Department for Work & Pensions (DWP) data

Table 3 shows that by the end of 2027-28, pensioners on the full rate of the **new** State Pension will be entitled to an annual amount that is above the income tax personal allowance. This means that they will be paying 20% income tax on the amount above the income tax personal tax allowance. By the end of 2029-30, an increase in the full rate of the **new** state pension of £1,727.63 will mean pensioners on the full rate receiving an additional amount of £1,702.21 (after income tax).

As with pensioners of the basic State Pension, some pensioners on the **new** State Pension will currently be paying income tax on their **new** State Pension; because they are entitled to an amount higher than the full rate<sup>13</sup> they may be receiving an amount that is above the income tax personal allowance.

Around one in thirty-three (3%) pensioners in receipt of the **new** State Pension currently receive an amount that is above the income tax pension allowance. With around half of pensioners in receipt of the **new** State Pension receiving the full rate this is expected to rise towards approaching three in five (55%) by the end of 2029-30.

Table 4 shows the proportion of pensioners in receipt of the **new** State Pension whose amount received is higher than the income tax personal allowance. This may be because they are in receipt of a delayed (deferred) State Pension and/or have protected payments from the previous system. The figures are presented for the three years 2021-22, 2024-25 and 2029-30<sup>12</sup>.

Table 4: Proportion and number of pensioners in receipt of the new state pension whose amounts received are higher than the income tax personal allowance

	2021-22	2024-25	2029-30
Proportion	1%	3%	55%
Number	0.02 million	0.1 million	1.9 million

Source: Author's calculations using on Department for Work & Pensions (DWP) data

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<sup>13</sup> Because they are in receipt of a delayed (deferred) State Pension and/or have protected payments from the previous system

Table 4 shows:

- in 2021-22, when the income tax personal allowance was raised to £12,570, around one in a hundred (1%) pensioners in receipt of the **new** State Pension received an amount that was above the income tax pension allowance. This equated to around 0.02 million such pensioners.
- in 2024-25 (today), with the income tax personal allowance having been kept at the same level, around one in thirty-three (3%) pensioners in receipt of the **new** State Pension are receiving an amount that is above the income tax pension allowance. This equates to around 0.1 million such pensioners; an increase of around 0.08 million such pensioners since the allowance has been kept at the same level.
- in 2029-30, the last possible year in which the next General Election can be held, over one in two (55%) pensioners in receipt of the **basic** State Pension are estimated to receive an amount that is above the income tax pension allowance. This equates to at least 1.9 million such pensioners; an increase of at least 1.8 million such pensioners from today and at least 1.88 million such pensioners since the allowance has been kept at the same level.

## The State Pension – basic & new together

Table 5 shows the proportion of pensioners in receipt of either the **basic** and the **new** State Pension whose amount received is higher than the income tax personal allowance. The figures are presented for the three years 2021-22<sup>111</sup>, 2024-25 and 2029-30<sup>12</sup>.

Table 5: Proportion and number of pensioners whose amounts received are higher than the income tax personal allowance

	2021-22	2024-25	2029-30
Proportion	4%	11%	43%
Number	0.5 million	1.4 million	5.5 million

Source: Author's calculations using on Department for Work & Pensions (DWP) data

Table 5 shows:

- in 2021-22, when the income tax personal allowance was raised to £12,570, around one in twenty-five (4%) pensioners received an amount that was above the income tax pension allowance. This equated to around 0.5 million such pensioners.
- in 2024-25 (today), with the income tax personal allowance having been kept at the same level, around one in ten (11%) pensioners are receiving an amount that is above the income tax pension allowance. This equates to around 1.4 million such pensioners; an increase of around 0.9 million such pensioners since the allowance has been kept at the same level.
- in 2029-30, the last possible year in which the next General Election can be held, over two in five (43%) pensioners are estimated to receive an amount that is above the income tax pension allowance. This equates to at least 5.5 million such pensioners; an increase of at least 4.1 million such pensioners from today and at least 5 million such pensioners since the allowance has been kept at the same level.



## Discussion

The decision to keep the income tax personal allowance at the same level since 2021-22 and rising it by inflation only from 2028-29, at the same time as increasing State Pension amounts by the triple-lock, means that many more pensioners will be paying income tax on the amount of State Pension they receive.

By the end of 2029-30, the proportion of pensioners in receipt of the **basic** State Pension to pay income tax on this amount is estimated to reach around two in five (39%) from around one in seven (13%) today and one in twenty (5%) when the income tax personal allowance was last changed. That is an estimated rise of at least 2.4m pensioners in receipt of a **basic** State Pension amount that will be liable for income tax (from around 1.2 million pensioners today to at least 3.6 million by the end of 2029-30); and from when the income tax personal allowance was last change at least an additional 3.1 million such pensioners.

By the end of 2029-30, the proportion of pensioners in receipt of the **new** State Pension to pay income tax on this amount is estimated to reach almost three in five (55%) from around one in thirty-three (3%) today and one in a hundred (1%) when the income tax personal allowance was last changed. That is a rise of at least 1.8 million pensioners in receipt of a **new** State Pension amount that is liable for income tax (from around 0.1 million pensioners today to at least 1.9 million by the end of 2029-30); and from when the income tax personal allowance was last change at least an additional 1.88 million such pensioners.

By the end of 2029-30, the proportion of **all** pensioners to pay income tax on their State Pension is amount is estimated to reach over two in five (43%) from around one in ten (11%) today and one in twenty-five (4%). That is a rise of at least 4.1 million pensioners in receipt of a State Pension amount that is liable for income tax (from around 1.4 million pensioners today to at least 5.5 million by the end of 2029-30); and from when the income tax personal allowance was last change at least an additional 5 million such pensioners.

The decision to keep the income tax personal allowance at the same level since 2021-22 and rising it by inflation only from 2028-29 means that by the end of 2029-30 at least an additional 5 million pensioners are estimated to receive a State Pension amount that is liable for income tax. That will be over two in five (43%) of all pensioners compared to around one in ten (11%) today and one in twenty-five (4%) when the income tax personal allowance was last changed.

Furthermore, the decision to keep the income tax personal allowance at the same level since 2021-22 and rising it by inflation only from 2028-29 means pensioners in receipt of the full rate of the new State Pension will receive an amount from 2027-28 that is above the allowance level and thus liable for income tax. The consequence for this is that from the end of 2027-28, pensioners in receipt of the full rate of the new State Pension, will not receive the full value of the increase in the full rate as an element will be taxed. So, whilst the full rate of the new State Pension will increase by the triple lock the amount received by such pensioners will not<sup>14</sup>; breaking the spirit if not the commitment to the triple lock for some pensioners.

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<sup>14</sup> From the end of 2028-29, a 2.5% increase in the full rate of the new State Pension will result in a take home amount that is equivalent to a 2.4% rise

## Annex A – Methodology estimating proportion & number of pensioners in receipt of State Pension amounts that are above the income tax personal allowance

To estimate the proportion and number of pensioners in receipt of State Pension amounts that are liable for income tax we used the Department for Work & Pensions (DWP) administrative data on pension recipients by category and by amount. This data only covers Great Britain, and we are therefore not able to include Northern Ireland in our analysis.

The data used is for the period up to May 2023 and accessed through Stat X-plore. DWP have suspended publication of more recent data because of internal processing issues, and we are therefore reliant on data from May 2023 as being the most up to date official dataset available.

The data presents the number of pensioners by receipt of basic State Pension and New State Pension by amounts received that are banded as follows: under £20, £20 to under £40, £40 to under £60, £60 to under £80, £80 to under £100, £100 to under £150, £150 to under £200, £200 to under £250, £250 to under £300, £300 and over.

The £12,570 income tax personal allowance equates to £241.73 per week<sup>15</sup>. This means a pensioner in receipt of a State Pension above this amount will be paying income tax on the element of this amount that is above the income tax personal allowance.

The bands in the data mean we are only able to say all pensioners receiving a State Pension equal to or more than £250 per week are paying income tax on an element of this amount. Table A1 below shows the proportion and number of pensioners, by category of pension, that are in receipt of a State Pension amount of £250 per week or more in 2021-22. Table A2 shows the same figures for 2024-25.

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<sup>15</sup> Calculation is to divide £12,570 by 53 (to reflect number of weeks in a year)

Table A1: proportion and number of pensions in receipt of State Pension amount of £250 per week or more (2021-22)

	Basic State Pension	New State Pension	Total
Proportion	5%	1%	4%
Number	0.5 million	0.02 million	0.5 million

Table A2: proportion and number of pensions in receipt of State Pension amount of £250 per week or more (2024-25)

	Basic State Pension	New State Pension	Total
Proportion	13%	3%	11%
Number	1.2 million	0.1 million	1.4 million

By end of 2029-30, the full rate of the basic state pension will be £25.37 per week higher than today whilst the full rate of the new State Pension will be £33.11 per week higher. This means basic State Pension pensioners currently in receipt of between £216.36 and £241.73 and new State Pension pensioners currently in receipt of between £208.62 and £241.73 will receive an increase that is sufficient to take their State Pension amount above the income tax personal allowance threshold.

The bands in the data mean we are only able to say all pensioners receiving a State Pension equal to or more than £200 and less than £250 per week will become newly liable to pay income tax on an element of their State Pension amount. Table A3 below shows the proportion and number of pensioners, by category of pension, that are in receipt of a State Pension amount of equal to or more than £200 and less than £250 per week.

Table A3: proportion and number of pensions in receipt of State Pension amount equal to or more than £200 and less than £250 per week (2029-30)

	Basic State Pension	New State Pension	Total
Proportion	25%	52%	33%
Number	2.4 million	1.8 million	4.1 million

The bands in the data mean that we have:

- underestimated the number of pensioners paying income tax on their State Pension amounts in table A1 and A2
- overestimated the number who will become newly liable for income tax on their State Pension amount in table A3.

However, these limitations are small in comparison to not having reflected in the analysis that by the end of 2029-30 the number of pensioners will have increased (all in receipt of the new State Pension). Therefore, the figures in table A3 will be a substantial underestimate.