Hunt urged to raise savings tax thresholds: Baroness Altmann leads calls to ease stealth levy that makes it even harder for savers to fight inflation

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Jeremy Hunt is under pressure to spare millions of prudent savers from a 'stealth tax on steroids'.

Having endured years of paltry returns on their nest eggs, savers are finally starting to benefit as interest rates rise.

But in what amounts to an attack on self-reliance and thrift, even those with modest amounts set aside face tax bills on the interest they earn.

Former pensions minister Baroness Altmann last night led calls for the Chancellor to raise the tax thresholds on savings income – allowing savers to earn more before handing cash over to the taxman.

'It's about the principle of rewarding rather than punishing savers who have had such a rough ride for so long,' she said.

Stealth tax: Chancellor Jeremy Hunt is under pressure to raise the tax thresholds on savings income

Basic rate taxpayers can earn up to £1,000 in interest from their savings without having to pay tax, under rules introduced by George Osborne seven years ago when he was Chancellor.

The tax-free allowance for higher rate taxpayers is £500 while those paying the additional 45p rate have no allowance at all and therefore pay tax on all their interest.

Osborne said when announcing the personal savings allowance that those who have already paid tax on their salary 'shouldn't have to pay tax a second time when they save it'. But rising interest rates mean that is what is happening.

From tax-free interest on £70k to just £20k

Osborne's policy spared millions from being liable for tax on their savings.

At that time, with interest rates close to zero, it was far harder to earn interest income of £1,000 or even £500 a year and therefore become liable for paying tax.

A basic rate taxpayer would have needed a savings pot of close to £70,000, while the equivalent figure for a higher rate taxpayer was around £35,000.

But with interest rates rising, a basic rate taxpayer now needs just over £20,000 set aside before the tax kicks in, while a higher rate taxpayer would be hit with just £10,000.

Tax makes it harder to fight inflation

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More than 6m are expected to be facing tax bills on their interest for the first time in seven years. Hunt is being urged to raise the tax thresholds.

Altmann said: 'Particularly at a time when government desperately needs to curb inflation, it makes sense to try to encourage more people to save rather than spend so that demand for goods is dampened.'

She said that even though interest rates are rising, savers were still losing out in real terms as returns lag behind the rate of inflation.

'This means people lose real value in their savings and after tax they are losing even more,' she said.

Figures from investment platform AJ Bell show that the sums raked in by HMRC from the tax rose sharply in the 2022-23 financial year to £3.4billion – more than twice the £1.3billion recorded the year before.

But that covered a period which started when the Bank of England's benchmark interest rate was still less than 1 per cent.

Tax relief: Baroness Altmann (pictured) wants the Chancellor to allow savers to earn more before handing cash over to the taxman

So for the current fiscal year – with the Bank rate at 4.5 per cent and likely to rise to 5.5 per cent before the year is out – it is likely to be substantially higher.

That is partly due to more and more people being dragged into the higher 40 per cent tax threshold, which has been frozen even though inflation is eating into the value of earnings.

> *This is stealth tax on steroids*

Laura Suter, from AJ Bell, said: 'The Government is raking in more and more money from the average saver, as the combination of interest rate rises and frozen tax allowances mean that many will pay tax on their savings for the first time ever. This is stealth tax on steroids.

'Not only are people facing more tax on their main income as a result of income tax bands being frozen, they are being hit with tax on their savings too as they are nudged into the next tax bracket and see their tax-free Personal Savings Allowance cut in half or lost altogether.'