DRS TAX & BUSINESS ADVISORS

Savings Tax and ISA Changes from April 2027
Why Cash Returns May Become More Taxable Than You Think

1. What Is Changing from April 2027

From April 2027, the taxation of savings income becomes more fragmented. In addition to the existing personal savings allowance, standalone savings tax bands will apply to interest income for certain taxpayers. At the same time, ISA rules are tightened, limiting the flexibility many higher earners have relied upon to shelter returns.

The practical effect is that cash interest and fixed-income returns may become taxable earlier than many savers expect, particularly where employment income already consumes lower tax bands.

For higher earners and company directors, savings income must now be viewed alongside salary, dividends and rental income, rather than treated as a separate pool.

2. How Savings Tax Works in Practice

Savings income is layered on top of non-savings income.

The order is critical:

1. Salary and other non-savings income use the personal allowance first.
2. That income then consumes the basic rate band.
3. Savings income is taxed according to the remaining band space.
4. The personal savings allowance applies, but only after band positioning is determined.

For higher-rate taxpayers, the personal savings allowance is £500. For additional-rate taxpayers, it is nil.

This means the effective tax rate on interest can move from 0% to 40% more quickly than many assume.

3. Modelling Scenario: Basic Rate vs Higher Rate Position

Assume:

- Salary: £48,000
- Interest income: £6,000
- Personal allowance: £12,570
- Basic rate band: £37,700

Salary after allowance:
£48,000 − £12,570 = £35,430

Remaining basic rate band:
£37,700 − £35,430 = £2,270

Interest layering:
First £2,270 taxed at 20%

Remaining £3,730 taxed at 40%
Personal savings allowance of £500 applies within the band position.

Tax calculation:
£5,500 taxable interest (after £500 allowance)

£2,270 at 20% = £454
£3,230 at 40% = £1,292

Total savings tax: £1,746

Effective rate on £6,000 interest: 29.1%

The taxpayer appears “basic rate” by salary, but the marginal rate on savings is significantly higher.

4. Interaction with the £100,000 Threshold

Savings income also forms part of adjusted net income.

Assume:
Salary: £98,000
Interest: £8,000
Total income: £106,000
Excess over £100,000: £6,000

Allowance reduction:
£6,000 ÷ 2 = £3,000
Loss of personal allowance creates additional tax:
£3,000 × 40% = £1,200

The £8,000 of interest may also be taxed at 40%.

Effective marginal impact on part of the interest can exceed 60% when taper interaction is considered.
Savings income is therefore not neutral for threshold-sensitive individuals.

5. ISA Changes and Capacity Constraints

ISAs remain one of the few environments where interest and investment growth are fully tax-free.

However, annual contribution limits remain capped, and restrictions on flexibility mean that many higher earners cannot simply “transfer” excess savings into shelter at short notice.

Assume:
Cash savings: £200,000
Average interest rate: 4.5%
Annual interest: £9,000

If fully taxable at 40%:
Tax cost: £3,600 per year

Over five years, assuming stable rates:
£18,000 cumulative tax leakage

If sheltered within ISA:
£0 tax

The opportunity cost of unused ISA allowance becomes more material as rates increase.

6. Five-Year Modelling: Taxable Savings vs ISA Shelter

Scenario A: Interest remains taxable

£9,000 annual interest
40% tax = £3,600 per year

Five-year tax cost:
£3,600 × 5 = £18,000

Scenario B: ISA shelter utilized

£0 tax
Full compounding retained

Difference over five years:
£18,000 direct tax saved

Plus compounding benefit on retained interest

This modelling becomes even more powerful where returns are reinvested rather than withdrawn.

7. Corporate Cash and Director Loans

For company directors, the position is more complex.

Where surplus cash sits within a company earning interest:

- Corporation tax applies to the interest income.
- Extracting that interest later as dividend creates second-layer taxation.

Effective combined rates can approach 50% or more depending on shareholder position.

Holding cash personally may create higher annual savings tax exposure but holding it corporately may create double taxation on extraction.

The correct answer depends on modelling future extraction strategy.

8. When Savings Structuring Becomes Critical

Savings planning becomes particularly important where:

- Total income is near £100,000.
- Dividend income already consumes the higher-rate band.
- ISA allowances have not been fully utilised historically.
- Large liquidity events are expected.

The interaction between savings income and thresholds can create unexpected marginal rates.

9. Key Takeaways

Savings income should no longer be viewed as passive or harmless.

When layered on top of employment and dividend income, interest can be taxed at 40% or more, and in some cases trigger personal allowance taper.

ISA capacity remains one of the most valuable shelters available, particularly in a higher-rate environment.

The difference between structured planning and reactive positioning can run into five figures over a relatively short period.

10. Talk to Us

If you hold significant cash balances personally or within a company, we can model:

- Interest layering across income bands
- Taper interaction
- ISA utilisation strategy
- Corporate versus personal holding comparison
- Five-year cumulative tax impact

A structured review before April 2027 can materially reduce avoidable tax leakage.

If you would like to begin reviewing your Tax and ISA modelling, you can:

- **Email:** info@drs-tax.com
- **Telephone:** 020 8059 1891
- **Submit an enquiry** via our Contact Us page
- **Book a free 15-minute consultation**