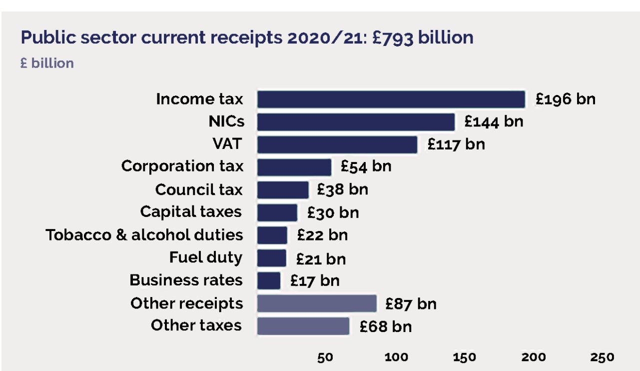
STRATEGIES AND TACTICS TO OPTIMISE RETURNS

Wherever there is a discussion about wealth, you can be sure that the word 'tax' is never far away.

Every year, the UK government raises close to £800bn from various tax sources, which is equivalent to around 37% of the size of the UK economy. The amount of tax we pay can have a significant impact on the 'real' value of our wealth, whether talking about our income and investments or our savings and assets.

This can be positive, in terms of tax relief, for example, or it might leave us with less than we expected after having to take into account any relevant tax obligations that must be paid to HM Revenue & Customs. And the higher your earnings, the more you can stand to lose or gain.



The complexities of the tax ecosystem can make it appear a daunting place, with a variety of thresholds, allowances and limits to navigate. There are, however, a number of advantageous routes that can make the journey more comfortable. This includes efficient ways to maximise your savings and effective channels to ensure your liabilities are limited to no more than the amount for which you are responsible.

Tax-efficient financial tools

One of the most straightforward ways to limit your tax liability is by investing in an Individual Savings Account (ISA), which comes in four forms: a cash ISA, a stocks and shares ISA, an innovative finance ISA or a Lifetime ISA.

Individuals can pay in up to a maximum of £20,000 (for the 2022/23 financial year) and any interest generated or capital growth will be free from income or capital gains tax. You can also contribute up to £9,000 into a junior ISA, which provides a tax-free wrapper to invest in your child's future.

> "Over a lifetime an average household will pay £1,101,255 (in 2019-20 prices) in direct and indirect taxes.
>
> Taxpayers' Alliance

	Annual deposit limit	Notes	Government bonus
Cash ISA	£20,000	Up to £85,000 protected under the Financial Services Compensation Scheme (FSCS)	No
Stocks & Shares ISA	£20,000	Risk-based investment, not protected by FSCS	No
Lifetime ISA	£4,000	Must be aged 18-39 when opening	Yes, 25%
Innovative finance ISA	£20,000	Higher risk, not protected by FSCS	No
Junior ISA	£9,000w	Separate from adult ISA allowance, children can't access money until 18.	No

Long-term thinking for later life

From a tax perspective, pensions are a highly effective way of investing to support your retirement. Individuals typically benefit from an annual allowance of £40,000 that can be invested for later life free from income tax and CGT.

Pension savings attract tax relief from the government according to your income tax bracket. That means basic-rate taxpayers receive 20% tax relief, while qualifying higher-rate and additional-rate taxpayers will be able to claim 40% and 45% respectively through Self-Assessment. Allowances that are unused within the last three tax years can benefit from carry forward if certain conditions are met and contributions are capped at 100% of annual earnings.

For higher earners, there are additional considerations to ensure your pension investment doesn't tip over the annual allowance limit. For example, every £10,000 earned over £240,000 will reduce the annual allowance by £5,000, and there is also a lifetime allowance – currently capped at £1,073,100 – which if exceeded will result in a life time allowance tax charge.

Tax benefits from backing business

The government has established a range of tax-friendly venture capital schemes designed to encourage investment into early-stage business. This includes the Enterprise Investment Scheme (EIS), the Seed Enterprise Investment Scheme (SEIS) and Social Investment Tax Relief (SITR) scheme as well as Venture Capital Trusts (VCT), all of which offer a minimum of 30% Income Tax relief and 50% in the case of SEIS.

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Around £75 billion was subscribed to Adult ISAs in 2019 to 2020.

HMRC

Scheme	Maximum annual investment you can claim Income Tax relief on	Percentage of investment on which you can claim Income Tax relief	Tax relief on income from dividends	Personal Capital Gains Tax relief available on your initial investment	Type of Capital Gains Tax relief on initial investment	Gains exempt from Capital Gains Tax when you sell shares	Relief available for capital losses against income
EIS	£1 million (£2 million if at least £1 million of that is invested in knowledge-intensive companies)	30%	No	Yes, on 100% of investment	Deferral	Yes, if you received Income Tax relief	Yes
SEIS	£100,000	50%	No	Yes, on 50% of investment, capped at £50,000	Exempt from tax	Yes, if you received Income Tax relief	Yes
SITR	£1 million	30%	No	Yes, on 100% of investment	Deferral	Yes, if you received Income Tax relief	Yes - but not on loans
VCT	£200,000	30%	Yes	N/A	N/A	Yes	No

Taking a holistic view

Viewed in isolation, ISAs, pensions and venture capital schemes are all powerful tools for minimising your exposure to tax and maximising the returns on your money. It's possible to multiply their tactical advantages, however, when they form part of a holistic strategy for tax-efficient investing.

Admittedly it presents a more complex proposition, but such a multi-layered approach can bring each tool to bear in a way that supports both your ongoing cashflow requirements and longer-term financial planning in the most tax-efficient way.

It enables you to zoom out and bring the context of your wider family situation into view so that sharing allowances can be optimised and any synergies with financial legacy planning can be considered. For example, you can avoid paying Inheritance Tax on gifts of up to £3,000 each tax year without them being added to the value of your estate, while gifts to spouses or civil partners are fully exempt from Inheritance Tax irrespective of their value.

These examples give an indication of the many strands that influence how much tax – or tax relief – an individual can be liable for. It is only with a proper understanding of your own personal circumstances and financial ambitions that it is possible to knit those strands together into a coherent, tax-efficient investment strategy that is truly fitted to you.

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