3D Financial Planning
Independent Financial Advisors

Tax efficient investments

This guide summarises some of the options for individuals who want to invest in a tax-efficient way.

Tax efficient savings and investments exist to help you make the most of your money by attracting tax relief. There are several tax breaks available, each working in a slightly different way, but all designed to encourage saving and make it more worthwhile.

New Individual Savings Accounts (NISAs)

One of the most popular tax efficient vehicles, ISAs replaced the more complex Personal Equity Plans and Tax Exempt Special Savings Accounts in 1999.

They are not an investment in themselves but are more of a wrapper that you can use to shelter any money invested within it from tax. There used to be two main types of ISA – cash and stocks and shares – but, on 1 July 2014, a New ISA (NISA) was introduced.

From 1 July 2014 you have been able to split the amount you invest between a cash or stocks and shares NISA as you choose, as long as you don't go over the overall annual limit of £15,000 (2014/15 tax year).

This means that you can now hold cash tax-free within your stocks and shares NISA, although you may still prefer to hold separate accounts for cash and stocks and shares.

You can open 1 cash and 1 stocks and shares NISA each year. You can choose to split your NISA investments how you wish. You can also now transfer investments held in a stocks and shares NISA into a cash NISA, which you weren't previously able to do.

Any interest earned in a cash NISA is free from income tax and investments in stocks and shares NISAs are free from both income and capital gains tax. Annual NISA allowances are aligned with the tax year. Any allowance that is not used within that tax year cannot be carried forward.

Junior ISAs

Junior ISAs replaced the child trust fund (CTF) in November 2011. Unlike CTFs, the government does not contribute to a Junior ISA but gains are free from income and capital gains tax in the same way as NISAs.

Junior ISAs are only available to those not eligible for a CTF. The maximum that can be invested per tax year increases in-line with inflation and is £4,000 for 2014/15.

As with NISAs, cash and stocks and shares can be held in a Junior ISA and the allowance can be split in any proportion between the two.

Once a Junior ISA has been opened anyone can contribute into it but no withdrawals are permitted until the age of 18, when the account becomes an 'adult' NISA.

If you are saving anyway, it is always worth considering making the most of this tax efficient annual allowance.

Contact us to discuss your options.

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Pensions

As average life expectancies increase and with ongoing low interest rates, investing for your future has never been more important. You could spend more than 30 years in retirement, which means a lot of saving is required to provide the income you'll need.

The government is keen to encourage pension saving and there is a generous tax relief attached to pension contributions.

Pensions tax relief

The tax relief you receive on your pension investments will depend on whether you are a basic, higher or additional rate taxpayer. Those paying a basic rate of 20% will be eligible for tax relief of the same amount, and the same goes for the higher rate of 40% and additional rate of 45% (2014/15 tax year).

The way the tax relief is applied to your pension investments will depend on the type of pension you pay into:

Occupational or public service pension schemes

Your employer will usually take the pension contributions from your pay before deducting tax but not national insurance. You then pay tax on what's left and effectively get the full relief straight away, whether you are a basic, higher or additional rate taxpayer. This is not always the case though.

Personal pensions

Through a personal pension you pay income tax on your earnings before any pension contribution.
The pension provider will then claim the tax back from the government at the basic rate of 20%. This means that you end up with £100 in your pot for every £80 you pay in. This also means that additional and higher rate taxpayers will need to claim the remaining tax relief through a tax return.

Contact us to find out how we can help you to consolidate and manage your pension savings.

Investing in small businesses

Venture Capital Trusts (VCTs)

VCTs are considered to be higher risk than other tax efficient investments because they involve investing in small, often start-up businesses that are not yet established. The tax relief that comes with VCTs reflects their high risk nature.

To encourage investment the government offers up to 30% income tax relief for subscriptions in new VCT fundraisings. You can invest up to £200,000 each tax year but the rebate is dependent on the amount of income tax you pay. You must also hold the shares for 5 years to keep the rebate.

When you dispose of a VCT after 5 years, any gain is exempt from capital gains tax and dividends paid by the VCT are also tax free.

VCTs should not be used solely for their tax benefits. It is important to get professional advice to ensure that you understand the risks.

The Enterprise Investment Scheme (EIS)

The EIS is another higher risk investment scheme that offers tax relief at 30% of the cost of shares. Again the risk comes from small, start-up businesses and the tax relief is dependent on your income tax liability in the tax year the investment is made.

The maximum investment eligible for relief is £1,000,000, which means the maximum tax reduction in any 1 year is £300,000.

There is also no capital gains tax to pay when you sell provided you keep your shares for at least 3 years.

The Seed Enterprise Investment Scheme (SEIS)

The SEIS provides income tax relief of 50% for individuals who invest in qualifying companies. The maximum annual investment is £100,000 and the rules mirror those of the EIS.

Like VCTs, both the EIS and SEIS are high risk investments and professional advice should be sought before investing. Please contact us.