INVESTMENTS • ADVICE • PLANNING

# Tax saving tips

Recent changes in the UK tax regime have highlighted the importance of clients reviewing the structure of their current and potential investment vehicles. It might not always be possible to avoid taxation of income or capital gains, but if the correct action is taken, the overall tax paid can potentially be reduced, letting you, the investor, benefit more from returns. There are so many considerations when deciding what action should be taken, and as tax legislation changes, you may find your investments could be structured in a more advantageous manner.

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## Tax Allowances Slashed

The capital gains tax exemption, dividend allowance and additional rate tax threshold were reduced in April 2023, with further reductions to the capital gains tax and dividend allowance flagged for April 2024.

## Implications For Investors

Reduced allowances have made it more difficult to achieve tax free, or tax efficient income and profits. Going forward, investment portfolios that are not held within a tax wrapper are now more likely to incur tax on income generated and gains crystallised.

Historically, individuals had a generous range of allowances to help mitigate potential tax liabilities. Recently announced changes will see more investors having to register for self-assessment to complete tax returns via HM Revenue and Customs (HMRC).

Very broadly (and dependant on the investments held), we would expect to see portfolios as modest as £25,000 start to incur tax on dividend income. The same £25,000 portfolio invested today, and disposed fully from April 2024, would only have to appreciate by 12% to trigger a capital gains tax liability.

## Relevant allowances are summarised below:

1. The tax-free dividend allowance has been reduced from £2,000 (2022-23) for the tax year, to £1,000 from April 2023 and then £500 from April 2024.
2. The capital gains tax allowance has been reduced from £12,300 (2022-23) for the tax year, to £6,000 from April 2023 and then £3,000 from April 2024.
3. Dividends received above the dividend allowance have had the taxation rate increased to 8.75% for basic rate taxpayers, 33.75% for higher rate taxpayers and 39.35% for additional rate taxpayers.
4. The £1,000 for Savings Interest (Basic Rate), £500 (Higher Rate), £0 (Additional Rate) are unchanged.

## Tax-efficient Structures

As always, personal circumstances and objectives will determine the most suitable way forward. Fortunately, there are a handful of investment options and 'tax wrappers' that can help investors reduce, and in some cases, remove any liability to income and capital gains tax. A tax wrapper is simply a vehicle that can be wrapped around a portfolio of assets and determines how the returns generated will be treated for tax purposes.

Which tax wrapper will be most beneficial (or a combination of) will be dictated by the size of the portfolio, your current tax position, anticipated tax position in the future, objectives for the funds, and cost and ease of access required. Given the nuances of choosing appropriate tax wrappers, it's important to seek professional financial advice.

## While not an exhaustive summary, here's some of the common structures (and the key features) that we use with our clients:

### Individual Savings Accounts (ISAs)

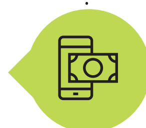
There are thousands of 'ISA millionaires' in the UK - those that enjoy tax exempt returns on a substantial investment portfolio, having utilised their annual allowance over many years.

- You don't pay tax on the growth, returns or interest in your ISA.
- All interest earned in the ISA is always tax free. You don't pay tax on any dividends from shares, and you don't pay capital gains tax on any profits made from the investments.
- At the moment, the annual allowance for ISAs is £20,000 per person. This means that between a married couple, they could put £40,000 per annum into this tax efficient environment.

### Investment Bonds

Investment bonds give the potential for capital growth, while still allowing you to make withdrawals. Investment bonds are non-income producing investments and can provide valuable tax planning opportunities for individuals. They are usually classed as a single premium 'life insurance' policy because a portion of your 'life insurance' policy can be paid out upon death, but they're really an investment product.

Investment bonds mainly fall into two categories, **onshore** and **offshore**. The main difference is their tax treatment. In high-level terms, those onshore are subject to UK corporation tax, which is offset by your provider, while offshore bonds are issued from outside the UK and the returns roll up gross of tax in the funds.



### Onshore Investment Bonds

- Also referred to as life assurance bonds, the funds underlying the bond are subject to UK life fund taxation meaning that you're treated as having paid income tax at the basic rate on the amount of your gain. You will have no liability to capital gains tax or basic rate income tax on bond gains. There is potential for further tax due for those with higher tax rates.
- You can withdraw up to 5% each year of the amount you have paid into your bond without paying any immediate tax on it. This allowance is cumulative so any unused part of this 5% limit can be carried forward to future years (although the total cannot be greater than 100% of the amount paid in). You will often see this referred to as the "5% tax-deferred allowance".
- The reporting requirement for taxation is on chargeable events. Chargeable events are commonly withdrawals/a disposal above the tax-deferred' allowance, death of the lives assured, or on maturity if a term is stated.
- Onshore investment bonds provide the ability to defer tax on profits to a point in time where the individual expects to have a lower marginal rate of tax. They also allow you to transfer segments of the bond to those with an insurable interest (such as children or grandchildren) for assessment at their marginal rate, again with basic rate tax deemed to have already been paid.

### Offshore (International) Investment Bonds

- These structures are usually based in tax privileged locations (offshore) such as the Isle of Man and Dublin.
- Profits generated by funds within the bond are generally free of tax, allowing the funds to grow year-over-year, benefiting from 'gross roll-up'.
- The lack of tax on an offshore bond means that potentially it could grow faster than one that is onshore, although this isn't guaranteed and the effect of other factors, such as charges, need to be considered.
- In line with their onshore counterparts, offshore investment bonds allow for the 5% tax-deferred allowance, so withdrawals can be made at a time that allows for a lower amount of tax to be paid - they can provide significant tax advantages where investments are held long term.
- Offshore bonds allow a wider variety of investments to be used, allowing for a diversified portfolio to be constructed, that can also be managed in a bespoke manner. Given gains are generally free of tax, changes to underlying portfolios where required can also be instructed without tax penalties.
- Offshore investment bonds are suited to larger portfolios, because there are increased administration costs associated with tax wrapper.

## Review Your Financial Plan with MHA Caves Wealth

If you would like to discuss prioritising tax efficiency, review an existing investment portfolio, or if you are thinking about establishing new investments, please contact us on **01604 621 421.**

Alternatively, you can contact us via email at **enquiries@mhacaves.co.uk** to arrange a free initial consultation.

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