WISE INVESTMENT

TAX YEAR ALLOWANCES

Happy New Year! As we tick over to another calendar year, we at Wise Investment are already well underway with our planning to help clients through the new tax year, for which the ball drops midnight on the 6th of April 2023.

With the new tax year, comes a new set of allowances. But also importantly, it means now is the last opportunity to use up some of this tax year's allowances, as they are in most part lost with the start of the new tax year.

Here we will run through the allowances for this year and next and important things to consider for both the run up to the end of this and the start of the next tax year.

ISAs and Junior ISAs

ISAs are often a key element of our clients financial planning, as they are a tax-efficient account, with any ongoing growth and income being exempt from tax. Furthermore, when you withdraw the proceeds, this is also free from tax. Because of this, the amount you can pay in annually is restricted.

The standard ISA allowance for UK residents is £20,000 this and next tax year. You can use your allowance by adding new money, or by moving existing investments. This can either be via a Stocks and Shares ISA or a Cash ISA.

You must be 16 or over for a Cash ISA and 18 or over for a Stocks and Shares ISA. The ISA allowance is a "use it or lose it" allowance and there is no opportunity to backdate any unused allowances.

For those that have maximised their own allowance, you can also invest on behalf of your children, or grandchildren with a Junior ISA (JISA), investing for their future, perhaps to help them out with university fees or toward a deposit on their first home. Under 18s have a JISA allowance of £9,000 per tax year. This means that 16 and 17-year-olds currently get two allowances - £9,000 for a JISA and £20,000 for an 'adult' Cash ISA.

Pensions Annual Allowance – Defined Contribution Schemes

With the introduction of Auto Enrolment in 2012, many people are beginning to realise the benefits of pension investments and it can be the cornerstone of one's retirement planning. Like ISAs, growth inside of a pension is tax free. Furthermore, any personal contributions you make, could receive up to 60% tax relief. There will be tax to pay at the point you take the benefits but this is likely to be at a significantly lower rate. Depending on how you take benefits, usually 25% is tax free and the remainder is subject to income tax.

Finally, in most cases, pension benefits are not subject to Inheritance Tax (IHT).

The amount you are permitted to contribute personally to a pension each year is the value of your earned income up to a maximum of £40,000 gross (£32,000 net of basic rate tax).

Earned income is classed as one or more of the following types of income:

- Employment income, such as: pay, wages, bonus, etc.
- Income from self-employment or a partnership
- Redundancy payment above the £30,000 tax exempt threshold
- Income from a UK and/or EEA furnished holiday lettings business

Pension income, Capital Gains, other rental income and investment income is not classed as earned and cannot be included here.

The rules differ slightly for employer contributions. They are still subject to the £40,000 limit but Employer contributions are not tested against your earnings, so more than 100% of your earnings can be contributed.

Employer pension contributions are paid gross by an employer and are normally treated as an allowable business expense. Consequently, they reduce the company's taxable profit, and so normally also reduce the company's Corporation Tax bill. However, HMRC guidance states that employer contributions can only qualify for Corporation Tax relief if they are judged to be "wholly and exclusively for the purposes of the trade".

Unlike ISAs it is possible for you to use any allowances you have missed for the 3 years preceding the current tax year, but for personal contributions, this can only be up to the maximum of your total salary for the current year. This is known as "carry forward" and it has a set of complex rules associated with it. We can discuss this with you and explain how this rule works, please let us know if you think this may apply to you.

There is another often unknown benefit of pension contributions for those with income over £100,000. At this level, your tax-free personal allowance tapers away at a rate of £1 for every extra £2 that you earn. This means your personal allowance is zero if you earn £125,140.

It's possible to use pension contributions to reduce or avoid a reduction in your personal allowance, meaning you'll pay less basic rate tax at 20%.

You could also receive up to 40% tax relief on your contributions over £100,000, resulting in effective tax relief of up to 60% on your contributions.

There are some exceptions to pension allowance rules, shown below.

If you don't have earned income (or earn less than £3,600 each year), you can still contribute up to £3,600 gross (£2,880 net).

If you have already taken taxable pension benefits flexibly via a drawdown arrangement, your allowance is reduced to £4,000 a year instead of £40,000.

Your annual allowance is also reduced if you earn more than £240,000 in the tax year, but you could still use the carry forward option, if applicable.

Please note if you are over 75 you won't qualify for tax relief on pension contributions. For this reason, most providers will not accept new contributions from customers aged 75 or over.

Any contributions made over your allowance, will be subject to the Annual Allowance Tax Charge, which effectively removes the tax relief you would have received on the contributions.

Capital Gains Tax (CGT) Allowance - £12,300

You can make capital gains of up to £12,300 without having a Capital Gains Tax liability. Sales of investments held outside ISAs, pensions and investment bonds may realise gains, as will any sales of property (other than your main private residence) or other assets you hold outside of tax-efficient wrappers.

We at Wise Investment help our clients to utilise any gains within their investments to make sure we maximise this available allowance where possible. It will be particularly important to do so this tax year as the allowance will be slashed to £6,000 next tax year and just £3,000 the year after.

Dividend Tax Allowance - £2,000

The dividend tax allowance remains at £2,000 per person and applies even if you choose to reinvest your dividends. Dividends generated by ISA and pension investments are exempt.

Again, some management and structuring of investments, can help make sure that these allowances are utilised. However, there will become less opportunity to do so as the allowance is to be halved to £1,000 next tax year and then to £500 the year after.

So, there is plenty to consider in the next few months, but the clock is ticking to make the most of your allowances.

This article is based on current Legislation. As we saw with the autumn statement in November, things can change very quickly, so if you would like to discuss any of the above with us, please get in contact.

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