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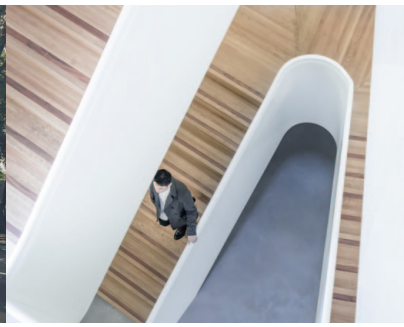

Tax-efficient investments

PENSIONS

Pensions remain a tax-efficient investment. Contributions to a pension scheme currently receive full tax relief at an individual's marginal rate, with the Government contributing 20% direct to the pension fund and the remaining tax relief being claimed on a Tax Return.

Income and gains within a pension fund grow tax-free. With the use of a Self Invested Personal Pension (SIPP) or a Small Self Administered Scheme (SSAS) an individual can retain a much greater level of control over investment decisions of the funds. A SSAS also offers additional benefits, such as the ability to lend money back to your own company.

There is now a great deal of flexibility over the withdrawal of benefits from pension funds. An individual can start to withdraw funds from age 55, and there are now no restrictions on the amount that can be withdrawn. The 25% tax-free withdrawal is still available.

Further, on death unused pension funds can be left to beneficiaries free of inheritance tax, and in some circumstances those beneficiaries can withdraw funds free of income tax.

While withdrawals from pension funds are very flexible, it has become increasingly difficult to invest in pensions without tax penalties. Many individuals can invest £40,000 per year, and it is still possible to utilise unused relief from earlier years. However, some individuals can only invest £10,000 per year. Employer contributions, auto-enrolment contributions and the accumulation of benefits under a final salary scheme all count towards an individual's limit. Great care must be taken if charges are to be avoided.

Finally, the value of an individual's total pension benefits must not exceed £1,055,000. If this limit is exceeded there are financial penalties.

ENTERPRISE INVESTMENT SCHEME

Investment in shares through the Enterprise Investment Scheme (EIS) attract significant tax benefits.

Any investment attracts tax relief at 30% and any profit on the sale of the shares in due course is free of capital gains tax. A capital gain on the sale of any assets (a buy-to-let property, for example) can be deferred into EIS shares, delaying the payment of capital gains tax. EIS shares also qualify for Business Property Relief, so should not be liable to inheritance tax should they be held at death.

If an investment in an EIS company should result in a loss, that commercial loss (net of income tax benefits) can be set against income so that further tax relief can be received.

The reason that EIS shares attract such tax benefits is because EIS investments are generally in high-risk businesses, and advice should always be taken when making EIS investments.

SEED ENTERPRISE INVESTMENT SCHEME

The Seed Enterprise Investment Scheme (SEIS) works in a similar way to EIS, but with additional tax benefits. The tax relief available on investment is 50%, and it is possible to eliminate part of recent gains by investing in SEIS shares. The reason for these additional tax benefits is that SEIS is only available when investing in small start-up businesses, and these investments are therefore considered higher risk.

VENTURE CAPITAL TRUSTS

Venture Capital Trusts (VCTs) are funds that are listed on the London Stock Exchange. These funds invest in small, high-risk businesses.

Any investment attracts tax relief at 30%, any dividends received are tax-free, and any capital gain on sale is tax-free.

It is not possible to defer gains or claim loss relief against income using a VCT, as with EIS.

BUSINESS INVESTMENT RELIEF

Business Investment Relief (BIR) is available to UK resident, non-domiciled individuals, and is designed to encourage the investment of funds in UK businesses. The relief allows a non-domiciled individual to bring funds to the UK without triggering a remittance, provided that the funds are invested in a qualifying company. Once the investment has matured the funds must be removed from the UK or further qualifying investments made if a charge to tax is to be avoided. Any gains or income received from UK investments will be liable to UK tax and can remain in the UK.

INVESTORS' RELIEF

Investors Relief is a new relief introduced from March 2016. This relief allows an individual to pay 10% tax on any gains made on subscribed shares in an unlisted trading company, where those shares are held for at least three years. For this purpose, unlisted includes AIM listed shares.

BUSINESS RELIEF FOR INHERITANCE TAX PURPOSES

On the death of an individual their estate is liable to inheritance tax at 40%, subject to the nil-rate band and any reliefs that can be claimed. Business Relief can enable an individual to receive 100% inheritance tax relief on funds that are invested in unlisted trading companies. For this purpose, unlisted includes AIM listed shares.

Business Relief portfolios are available from Financial Advisers, giving the ability for individuals to retain their wealth and receive IHT benefits.

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INDIVIDUAL SAVINGS ACCOUNTS

ISAs have been around since 1999. They initially offered the ability for a UK resident individual to invest a small amount each year and for that investment to grow free of income tax and capital gains tax. An ISA could hold cash, or stocks and shares.

STANDARD ISA

The Standard ISA currently enables an individual to invest £20,000 per year. These funds may be invested as cash, or as stocks and shares. Income and gains arising within an ISA are tax-free. Funds can be drawn from an ISA freely, and no accumulated tax benefits are lost. Further, withdrawn funds can be reinvested in the same tax year without using any of the £20,000 investment allowance, giving short-term access to funds with no loss of benefits.

The investment decisions of a stocks and shares ISA can be made by the ISA provider, or by the individual using a self-select ISA.

If an ISA is left to an individual's spouse on death the funds will retain their identity as an ISA and the tax-free status is preserved. They are, however, liable to inheritance tax in the normal way.

A standard ISA can only be opened if you are at least 18 years old (or 16 years old for a cash ISA).

JUNIOR ISA

A Junior ISA can be opened by the guardians of an individual that is too young for a Standard ISA. Funds may be invested as cash, or in stocks and shares. The annual investment limit is currently £4,368. Income and gains arise in the ISA free of income and capital gains tax.

Once funds are invested in a Junior ISA they cannot be withdrawn until the individual is 18 years old. They cannot be used for the maintenance of the child in any way. Once the individual is 18 years old the ISA converts into a Standard ISA and the funds can be withdrawn freely.

LIFETIME ISA

A Lifetime ISA can be opened by a UK resident individual aged between 18 and 40 years old. Up to £4,000 per year can be saved until the account holder is 50 years old. Any funds invested in a Lifetime ISA count towards an individual's annual £20,000 ISA investment limit. Funds can be invested as cash, or in stocks and shares. Each year a 25% bonus is paid on the amount saved in that year. Income, gains and bonuses accumulate in the ISA tax-free.

Funds can only be withdrawn from a Lifetime ISA without charge if the individual is buying their first home, has reached age 60, or is terminally ill. If none of these conditions are met any withdrawals will incur a 25% charge.

INNOVATIVE FINANCE ISA

The Innovative Finance ISA (IFISA) was introduced on 6 April 2016 to enable individuals to take advantage of the more attractive interest rates offered by peer to peer lending. Up to £20,000 per year can be invested in an IFISA. Any investments count towards an individual's overall ISA limit of £20,000 per year.

IFISA may offer more attractive returns, but are generally considered more risky.

MEET THE TEAM

If you require further information or guidance on any of the matters in this guide, do not hesitate to contact the Wilson Wright team.

For full details of our services please visit wilsonwright.com or call 020 7832 0444.

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