TAX YEAR PLANNING

2025/26

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BOOST YOUR EFFECTIVE INCOME: SMART TAX STRATEGIES

What is the simplest way to give yourself a de facto pay rise? To spend less of course - especially on tax. Naturally, it is only right that we all contribute our fair share to society, but the tax system offers incentives specifically to encourage saving and investing for the future. Are you taking full advantage of these opportunities?

THE IMPACT OF FROZEN TAX BANDS

With the main tax bands and allowances frozen until April 2028 (and even April 2030 for Inheritance Tax bands), inflation is causing 'fiscal drag'. This means that as incomes rise with inflation, more of your earnings fall into higher tax brackets, effectively increasing your tax burden even though your real-terms wealth may not have increased. In this environment, maximising available allowances becomes even more critical to keep your financial plans on track.

TIME FOR FINANCIAL HOUSEKEEPING

It's never too soon in the tax year to review your financial situation. Consider this your call to action:

1. Assess your current tax strategy
2. Utilise all available allowances and exemptions
3. Plan ahead for the upcoming tax year and beyond

By taking these steps, you can potentially retain more of your hard-earned money and set yourself up for a more financially secure future. Remember, effective tax planning is not about avoidance, but about using the system as it's designed to work for you.

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If you would like advice on planning your financial strategy, we would be happy to help:

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YOUR TAX ALLOWANCE CHECKLIST

Area	Allowance	Limit (2025/26)	Utilised for 2025/26?
Pensions	Annual Allowance	£60,000+ (or earnings if less)	☐
ISAs	Main Adult Allowance	£20,000	☐
Capital Gains Tax	Annual Exemption	£3,000	☐
Income Tax	Personal Allowance	£12,570	☐
	Dividend Allowance	£500	☐
	Personal Savings Allowance	£1,000 BRT / £500 HRT[1]	☐
Inheritance Tax	Annual Exemption	£3,000+	☐
	Normal Expenditure From Income	Excess income	☐
	Small Gifts	£250 per person	☐
	Nil Rate Band Gifting	£325,000[2]	☐
Tax Efficient Investments	Venture Capital Trust (VCT)	£200,000	☐
	Enterprise Investment Scheme (EIS)	£1m - £2m[3]	☐

1. BRT = Basic Rate Taxpayer, HRT = Higher Rate Taxpayer
2. Every seven years, and other strategies are available. All other limits are per tax year.
3. Standard limit £1m, higher limit of £2m applies for 'Knowledge-Intensive' investments

PENSION CONTRIBUTIONS

Pension contributions are generally the first port of call for anyone saving for income in retirement, offering a number of tax benefits:

- **Income tax relief is received on contributions**
- **Growth on the fund is largely tax-free**
- **Up to 25% of the fund can be taken as tax-free cash on retirement**

Even ignoring the potentially enormous benefit of largely tax free growth over decades, the table shows the net free-uplift offered by just the initial income tax relief and 25% tax free cash (the tax free cash amount being limited by the **maximum Lump Sum Allowance of £268,275**, or your own transitional amount if pension relief applies).

For example: If you are a higher rate taxpayer when making pension contributions, and a basic rate taxpayer in retirement, your savings would benefit from a massive 41.67% boost from the tax advantages afforded to pensions.

For those where even higher effective tax relief could apply (e.g. where effective rate tax traps are avoided, see page 7), the benefits can be even greater.

Taxpayer Basis (when saving)	Taxpayer Basis (in retirement)	Net Boost to Savings*
Basic rate (20%)	Basic rate (20%)	6.36%
Higher rate (40%)	Basic rate (20%)	41.67%
Higher rate (40%)	Higher rate (40%)	16.67%
Additional rate (45%)	Higher rate (40%)	27.27%
Additional rate (45%)	Additional rate (45%)	20.45%

*Ignoring the additional benefit of tax-free growth for the period invested, and based on current tax rates and legislation, which are subject to change. Assumes sufficient Lump Sum Allowance remains to enable 25% tax free cash to be taken. The rates and 'net boost to savings' are different if you are resident in Scotland.

WHAT ARE THE PENSION CONTRIBUTION LIMITS?

The amount you can contribute tax efficiently into a pension each year is limited by the **lower** of two figures:

1. The **annual allowance** which currently stands at £60,000 for most people. This is the cap on the amount of pension contributions you can make (or receive from e.g. your employer) in a tax year. However, up to three years of unused annual allowance can be carried forward to increase this limit if needed. **That means this tax year is your last opportunity to use any unused allowance from 2022/23**.

   If you have already taken benefits from a money purchase (also known as a defined contribution) scheme, beware that the reduced Money Purchase Annual Allowance (MPAA) of £10,000 (with no carry forward) may apply to you.

2. **Your annual earned income** – you are not able to claim tax relief on contributions higher than your earnings in a tax year. If the annual allowance (including carry forward) is lower than your earnings, your contribution is effectively limited by the annual allowance instead.

HIGHER EARNERS: BEWARE THE TAPERED ANNUAL ALLOWANCE

The decision to make pension contributions is complicated for 'high- earners' (very simplistically: those with taxable income (not just earnings) including all pension accruals, exceeding £260,000), with a taper applied to the annual allowance which may reduce this down from £60,000 to as little as £10,000, plus any available carry forward.

If you suspect this may apply to you, and you have not already taken action, please do contact us to examine your options before further contributions are made.

These rules can complicate pension contributions. Your clarity adviser can help determine what is both possible and desirable, for you to meet your goals.

THE LUMP SUM ALLOWANCE

Although there is no longer a Lifetime Allowance test on the total value of your pension savings, there are still limits applying to the level of tax-free lump sums which can be taken from pensions in lifetime and on death.

The Pension Commencement Lump Sum (tax free cash) amount available, when taking pension benefits, remains at a maximum of 25% of your pension fund value. This is subject to a Lump Sum Allowance limiting the overall amount which can be taken, which stands at £268,275. Those with pensions protection will have their own personal protected levels of Lump Sum Allowance.

If your pension fund and/or tax free cash taken is already above this threshold, then any new pension contributions will not benefit from additional tax free cash. However, you will still receive income tax relief at your highest marginal rate, and also benefit from tax free growth whilst the funds are invested in the pension.

PENSION PLANNING TIPS

OPTIMISING THE BALANCE OF RETIREMENT INCOME FOR COUPLES

If you're married or in a civil partnership, how much should each of you contribute to your own pension? Consider whether you will have sufficient pensions income for each of you to use at least both of your tax-free personal allowances in retirement, if not also your basic rate bands. In addition, there is the Lump Sum Allowance to make effective use of for both parties.

Making pension contributions for the lower earner of the couple can actually be more tax efficient, if the pension will be taxed at a lower or nil rate in retirement (see page 4). As detailed to the right, small contributions are even possible for those with no earned income

Your adviser can help you project forward your retirement plans to make sure your savings are landing in the best place for you. Speak to us about our WealthPlan modelling and forecasting tool if this would be of interest.

PENSION CONTRIBUTIONS FOR INTERGENERATIONAL PLANNING

Even if someone has no earned income and has paid no tax, they can still pay up to £3,600 per annum (gross) into a pension and receive basic rate tax relief on the contribution - so the actual amount paid is £2,880. This can be into your own or another's pension plan as a gift. This provides a great opportunity to consider a pension payment for non-working spouses, children or grandchildren.

An additional tax bonus for those gifting down the generations is that the gift can benefit from an IHT exemption using either the '**normal expenditure out of income**' exemption for regular gifts from excess income, or using the £3,000 annual exemption if not already used.

This allowance applies per person, so a couple could gift up to £6,000 each year, free from potential IHT considerations, and also carry forward a further £6,000 exemption from the previous year if unused.

PENSION PLANNING TIPS

AVOIDING EFFECTIVE RATE TAX TRAPS

There are some bands of income where the effective tax rate is far higher than the standard rate for that band, because additional allowances or benefits are also lost as your income moves through the band. If you are just above one of these bands, making pension contributions that reduce your taxable income can give you higher than marginal rate income tax relief.

Band £100,000 to £125,140: the tax-free personal allowance is reduced by £1 for every £2 that an individual's income exceeds £100,000 and is lost completely where income exceeds £125,140. This means that the effective rate of income tax in this band is 60% (40% higher rate, plus the amount of the personal allowance lost, also taxed at 40%). If you fall in or just over this band, making a pension contribution could reduce your taxable income and could gain you 60% effective tax relief. As mentioned earlier, if you are resident in Scotland then the tax rates are different and, at this margin, a pension contribution could gain you effective tax relief at 67.5%.

Band £60,000 to £80,000: if you receive **Child Benefit**, this is reduced by 1% for every £200 that the household high earner's income exceeds £60,000 and is lost completely over £80,000. Again, if you fall in or just above this band, you may find that making a pension contribution enables you to retain some or all of the Child Benefit. This can offer between 50% and 70% effective tax relief, depending on how many children you have. Again, different for those resident in Scotland.

INDIVIDUAL SAVINGS ACCOUNTS (ISAS)

Have you made use of your ISA allowance this year? You are able to place £20,000 per person in each tax year in this tax-free wrapper. If the allowance is not used in a year, it cannot be carried forward.

Regular use of your allowance over the years can result in a very large tax-free savings pot, which you can use to supplement your retirement income or work towards any of your other financial goals. As a simple example, if you invested the full allowance each year from age 26, you would be sitting on a pot worth over a million by the age of 50, assuming an average annual compound return of 6% - giving you the freedom to retire early, or for a mid-life career change.

ISAs don't offer any tax relief on investment, unlike pensions, but ISA funds grow in a similar tax-free environment, and there are no age restrictions or tax consequences when funds are withdrawn. They can make the perfect complement to pensions savings – perhaps to cover an anticipated period of retirement before pensions are accessible, or to provide extra tax free income in retirement. Or they have a multitude of uses for shorter term savings.

Once one of the simplest financial wrappers, there are now many different forms of ISA, each with their own rules and contribution limits.

Whatever you are saving for, there is an ISA for you and your clarity adviser can help you select the right one.

	Stocks & Shares	Cash	Junior	Lifetime (LISA)
Age Criteria	>18	>18	<18	Opening: 18- 40 Contributions: 18 - 50
Other Criteria	You can contribute to any number of stocks & shares ISAs and cash ISAs in each tax year		Cannot open alongside a child trust fund (CTF), but CTFs can be transferred into junior ISAs	Use only for: 1. first-time house purchase <£450k 2. after age 60 Other withdrawals mean the bonus is lost, and in addition an effective 6.25% penalty on your investment applies
Maximum Contributions (2025/26)	£20,000 (minus any payments made to other ISAs)		£9,000	£4,000
Government Bonus	Not applicable			Yes 25%

If your ISA is "Flexible", you can take any amount of money out and pay it back in again without impacting your contribution allowance. It is important that the payment back in is made to the same ISA that the withdrawal came from and the top-up contribution is made in the same tax year as the withdrawal.

Not all ISAs are Flexible, your provider will be able to provide confirmation.

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CAPITAL GAINS TAX (CGT) ANNUAL EXEMPTION

The capital gains tax exemption is currently £3,000. You are able to realise capital gains up to this amount before you start having to pay tax. The exemption must be used before the end of each tax year, it cannot be carried forward.

The rate of tax paid on capital gains, however, remains at relatively low levels compared to income tax rates.

	All disposals
Basic rate[1]	18%
Above basic rate[1]	24%

1. Gains falling into band, when added to other taxable income

CGT PLANNING TIPS

Transfers between married couples and civil partners are at 'nil-gain nil-loss'. Investments can be transferred between couples before sale so both allowances are used.

Care is needed if you realise both capital losses and gains during a year, as these have to be fully set against each other before use of the annual exemption. Careful planning is needed to ensure that the taxable benefit of capital losses is not wasted. If you do have net capital losses overall in a year, then these must be claimed on your self-assessment tax return to enable them to be carried forward. They can then be used to reduce overall gains in a future year, and in this case you are able to choose the amount to be used, so can preserve the use of the annual exemption.

What to do with the amounts realised? Share-matching rules mean you must not repurchase the same fund within 30 days of sale for it to 'count' for CGT purposes. The sale is an ideal opportunity to rebalance towards your target asset allocation. If you do want to repurchase the same fund, but minimise your time out of market, then you could consider strategies such as '**bed and ISA**', '**bed and SIPP**', or '**bed and spouse**' (less fun than it sounds). These strategies involve repurchasing the fund in an alternative wrapper or by a different person, in which case the 30 day rule does not apply.

See our Guide to Capital Gains Tax for more details of the calculation process and planning hints and tips.

Your clarity adviser can look at your overall position in the context of your present and future needs, and show you how your savings can be most efficiently invested.

INCOME TAX ALLOWANCES ✔

With income tax bands also frozen until April 2028, more of your income may be falling into higher rate tax bands, increasing your tax burden. Is your income structured in the most tax-efficient way possible?

Married couples and civil partners should consider whether you are using both of your personal allowances for tax-free income (£12,570 each), as well as both personal savings allowances and dividend allowances. Allowing for practical considerations, should assets be given to a lower or non-taxpaying spouse?

A **personal savings allowance** (effectively a nil rate band for interest income) is available of £1,000 for a basic rate taxpayer, and £500 for a higher rate taxpayer (nothing for an additional rate taxpayer). Care should be taken that a small move into the next tax bracket does not mean the loss of some/all of the allowance.

In addition, a similar dividend allowance is available of £500 for all taxpayers.

It is also possible to use **your child's personal allowances** by gifting assets to them, although care must be taken that a parental gift doesn't fall foul of anti-avoidance rules. Assets transferred by a parent to a minor, unmarried child are deemed to be taxable on the parent where income is earned over £100 per tax year. However, if a child receives a gift from elsewhere, grandparents for instance, any income is offset against the child's own personal allowance.

We can help with planning to ensure that dividends are arising in the most tax effective manner.

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INHERITANCE TAX (IHT) ✅ ALLOWANCES

IHT planning is an ever-greater concern for many of our clients. The nil rate band applying to estates on death has been frozen at £325,000 since 2008/09 and will now remain frozen until 5 April 2030, with the £175,000 residence nil rate band potentially also available (but also frozen).

Together these mean that the first £500,000 of an estate could be free from IHT, but **the real value of this nil rate amount is decreasing each year**. Any amounts over this are subject to IHT of 40%. With careful planning and regular use of the available exemptions and reliefs, the impact of IHT can be greatly mitigated. If you are considering making gifts, plan early.

Early planning is likely to become even more relevant for those who have planned to leave some of their pension funds as inheritances. Pensions do not generally fall into the estate for IHT at present, but it is proposed that IHT will apply from April 2027. Full details are yet to be announced, but those affected will no doubt want to discuss the consequences with their adviser at their next annual review.

PLANNING INTO THE FUTURE

For clients who wish to look a little further ahead, gifts (outright or into trust) can be made to start the seven-year clock ticking. Gifts of up to the nil rate band (£325,000) can be made from each individual, free from immediate tax, and can be repeated every seven years to build up significant assets outside of the taxable estate.

USING ANNUAL EXEMPTIONS AND RELIEFS

Unless you survive for 7 years after making a gift, IHT may effectively be payable on the gift. However, there are a number of small but often overlooked reliefs that can be regularly used to guarantee that gifts will remain free from IHT. These can be combined with gifting into pensions or ISAs for the recipient, for added tax efficiency.

- Each individual has an annual £3,000 exemption and can carry forward any unused portion of this exemption from the previous year. This can cover gifts to one or many individuals, and use of this exemption for a couple could cover up to £12,000 of gifts in a year if it has been previously unused.
- Normal expenditure out of income is a useful, but little used, relief. Regular gifts made from demonstrably excess income fall outside the estate immediately, without the usual seven-year time period applying. This is a perfect relief to use for making monthly pension contributions for the benefit of grandchildren, which would also benefit from basic rate tax relief (up to £240pm net). Or perhaps into a junior ISA to help grandchildren with university costs.
- Small gifts totalling less than £250 per year to each individual are also exempt (this can't be combined with other exemptions).

Your clarity adviser can help forecast finances, determine affordable gifting, structure gifts for tax efficiency and, where appropriate, recommend suitable investments.

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INVESTMENT ALLOWANCES: VCT AND EIS

If you have fully used your ISA and pension allowances and have excess funds to invest, have you considered whether other tax efficient vehicles could suit you? These might include venture capital trusts (VCTs), maximum allowance £200,000, or enterprise investment schemes (EISs), maximum investment £1m-£2m depending on the type of company. These offer 30% income tax relief on investments, and, with VCTs, the prospect of tax-free dividends.

They are not suitable for everyone, as the nature of the underlying investments and the restricted liquidity make them a high-risk option. However, the restrictions on pension savings mean that they are an increasingly popular part of retirement planning strategy for those able to take the investment risk.

New issues are likely to close quickly, so please do let us know as soon as possible if you would like guidance in this area.

Listen to our podcast episode on VCTs here

EXAMPLES OF CURRENT VCTS ON OFFER

Puma VCT 13

Launched in September 2017, this VCT focuses on scale-up companies rather than start-ups, reducing risk and volatility. Recognized as one of the top-performing generalist VCTs over five years as of August 2024, it has achieved a total return of over 57%. The fund's diversified portfolio includes over 20 companies across sectors such as Consumer Services, Business Services, and Fintech. Since inception, it has invested more than £70 million in UK qualifying businesses.

Octopus Apollo VCT

This VCT supports around 45 established B2B software companies with predictable, recurring revenues of £2-8 million annually. It avoids consumer-focused businesses, instead investing in companies operating for 4 to 10 years that have already brought their product or service to market. As one of the largest generalist VCTs, it aims to pay regular tax-free dividends of at least 5% of NAV per share annually, helping accelerate the growth of technology companies.

If you're interested in this kind of investment, please contact your usual clarity adviser.

Important information: Our views are based upon our understanding of current legislation in England, unless stated otherwise. Levels and bases of, and reliefs from, taxation are subject to change and their value to you will depend upon your personal circumstances. This document is provided for information only and does not constitute advice. You should not act on any of the information without seeking professional advice.

Risk Warning: The past is not necessarily a guide to future performance. The value of your investment and the income from it can fall as well as rise and is not guaranteed. You may not get back the full amount invested.