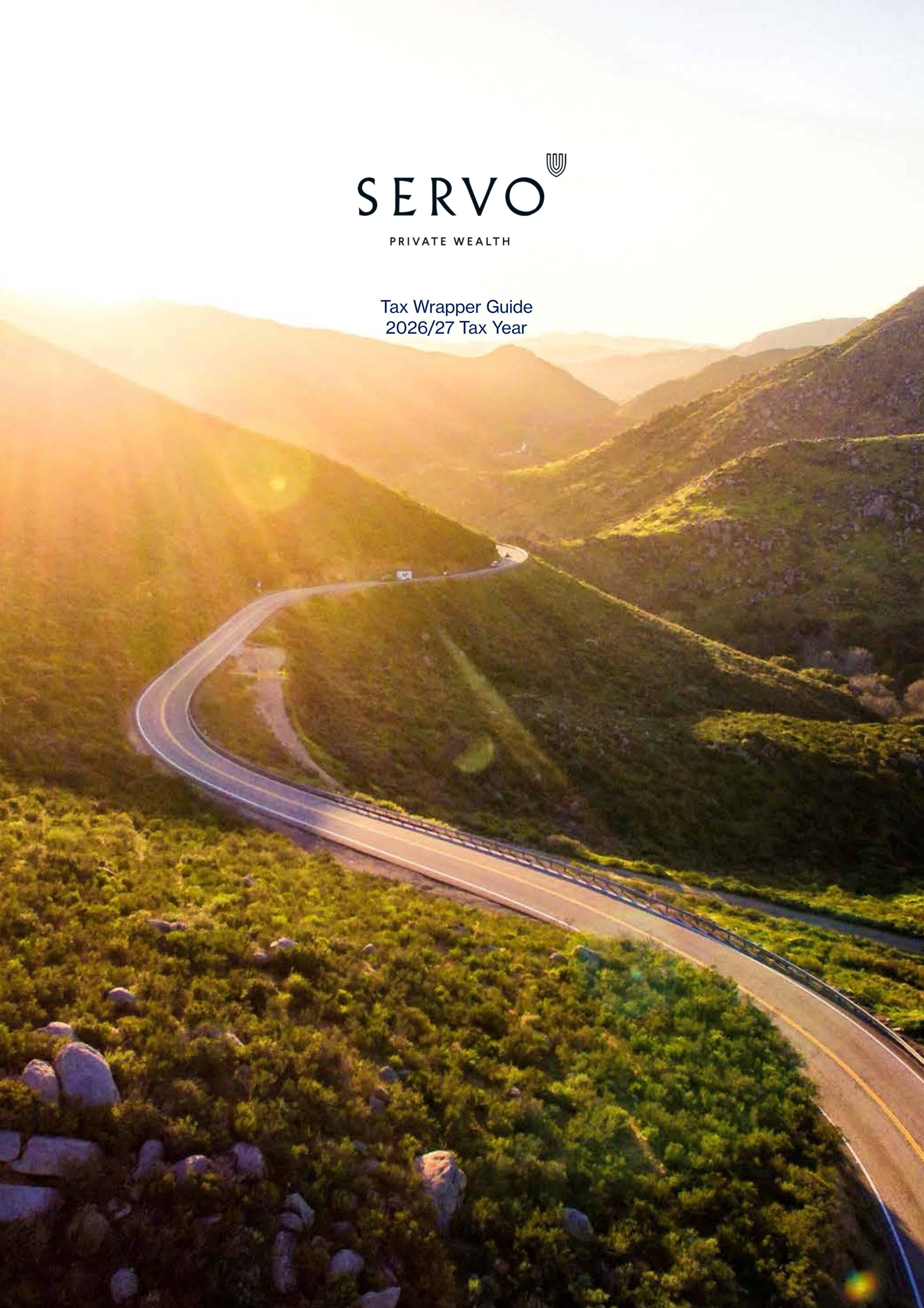
SERVO

PRIVATE WEALTH

Tax Wrapper Guide
2026/27 Tax Year



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INTRODUCTION

When we talk about investments with our clients, we often refer to **'tax wrappers'**. The most common tax wrappers we use in financial planning are:

- Individual Savings Accounts (ISAs)
- Investment bonds
- Pensions

A tax wrapper is not an investment in itself; rather it is an account that *wraps around* an investment (or cash) to change the way it is taxed – i.e. to give you additional benefits and/or help your investment grow faster. If your investment is not held within a tax wrapper, it is known as a 'directly held' or 'unwrapped' investment.

A General Investment Account (GIA) can also be used to hold 'unwrapped' cash and investments, and looks a bit like a tax wrapper, but it does not offer any tax sheltering; it is more of an administrative mechanism to invest or hold cash in a tidy and relatively flexible way.

This document gives you a brief overview of both unwrapped investments and the tax wrappers noted above, including their main features and benefits, based on the current legislation that applies at the time of writing.

WRAP ACCOUNTS AND PLATFORMS

Over the last 25 years, the financial services profession has seen the gradual introduction and rising popularity of online investment platforms, also known as 'wrap accounts', that enable you to invest in a wide range of funds and assets, across multiple tax wrappers.

These allow investors to hold all their investments and tax wrappers in one place, with online access to real time valuations and consolidated reporting.

This document does not specifically discuss wrap accounts, but we do regularly recommend them to our clients. We have separate guides available on request that outline why we believe platforms are suitable for most of our clients, as well as our providing our research into, and due diligence of, the wrap account market.

All the tax wrappers discussed in this document are available through most wrap accounts, as are GIAs.

DIRECTLY HELD STOCKS AND SHARES

'Investments' is a collective term for stocks and shares that are traded on stock markets, either in the UK or around the world. 'Stocks' and 'shares' are two different ways for companies to raise money, for example, to fund their growth plans or invest in research and development.

- **Stocks** are more commonly known as **fixed interest** investments in the financial serviced world, including **loan stocks, gilts** and **corporate bonds**. Stocks are like a personal loan, except you (the investor) are the 'bank' and the company you are investing in is the one taking out the loan. Stocks are referred to as 'fixed interest' because the company you are lending the money to pays a fixed level of interest to borrow that money.

  Depending on the financial strength of the company you are buying the stocks in, the interest rate (and any capital growth you may achieve) will be more or less attractive. The lower a company's financial strength, the higher the interest rate you would receive, because there is a higher risk that it could default on its payments. If, however, you bought stocks from the UK Government (which are called gilts), the interest rate would be lower because the UK Government would not, under normal circumstances, default on a debt. Therefore, Government bonds are known as 'gilt-edged' investments, due their historic perception of relative security.

- **Shares**, also known as **equities**, allow investors to *own* a share of that company. As a part owner of the company, you are entitled to vote at Annual General Meetings and have a say in how the company is managed, if you want to. Any growth achieved by the company (or in the company's perceived value) is reflected in the value of your shares going up. Any profits achieved by the company can be passed on to its shareholders by declaring dividends, which are variable in value and frequency.

  The growth potential for shares is generally higher than for stocks over the longer-term because, if a company winds up, stockholders will normally receive back the value of their loans before the shareholders receive any value. This is an example of 'risk and reward', where shares have greater long-term income and capital growth potential because you take more risk with them.
  Rather confusingly, in the US shares are known as 'stocks' and fixed interest assets are known as 'bonds'. These terms are now being widely adopted in the UK too.

There are three main ways you can invest in stocks and shares. These are:

- **Directly**, i.e. buying individual stocks and shares that you can manage either personally or via a stockbroker, usually through an online trading account. Older stocks and shares are often held on certificates rather than electronically through an online account.

- **Through a collective investment**, such as a Unit Trust, Open Ended Investment Company (OEIC), or Investment Trust. These are all forms of collective funds, each subject to their own legislation but sharing basically the same tax treatment.

- **Through a tax wrapper**, such as a pension, ISA or investment bond. Tax wrappers can hold stocks and shares directly or through collective investment funds.

COLLECTIVE INVESTMENT FUNDS (UNIT TRUSTS, OEICS AND INVESTMENT TRUSTS)

We do not normally advocate investing in stocks and shares directly, as it is a much higher risk way of investing in the stock market, and it requires more ongoing management. Your money would be held in one, or a small number of, individual companies, which means you are highly reliant on those companies continuing to do well. If they fall in value, more of your money would lose value, because a lot of it is held in one place. The one advantage of holding them directly is that they do not generally bear any ongoing charges, aside from dealing fees to buy and sell. However, the risk of their failure, and the extra time needed to manage them, far outweigh any costs, in our experience.

Collective funds provide the best solution, in our view. They are 'baskets' of stocks and/or shares in multiple organisations, wrapped up in a fund that can be easily bought or sold. It is not unusual for a collective fund to hold anything from 25 individual stocks and/or shares in a single sector, right up to well tens of thousands across multiple asset classes across the globe. This diversification is key to diluting risk in your portfolio. If one individual company fails or suffers a downturn, you are much less likely to be impacted by it when it is only a tiny part of your overall portfolio, than if you invested in that company directly through an individual shareholding. It also allows you to benefit from returns in other areas that you would not be exposed to if you only invested in a handful of direct shares.

It is common to hold a range of collective funds, for example concentrating on different asset classes (e.g. stocks, shares, commercial property or alternative assets), markets, geographic regions or investment styles. Together, they would form a very diverse portfolio that is able to weather different markets and economic conditions, and it is the approach we take in most cases.

GENERAL INVESTMENT ACCOUNTS (GIAS)

Historically, investors would have bought collective funds from a variety of investment houses, each with its own set of paperwork, fund range to choose from and valuation dates. This made it difficult to get an overall view of their investments in one place and at one point in time.

As noted earlier, in recent years, some investment houses and investment administration companies have launched **platforms**, also known as **wrap accounts**. These are like a fund 'supermarket' where you can invest in a wide range of collective funds, stocks, shares and cash through a single, online, investment account.

Through these platforms, investments and cash that are not placed inside a specific tax wrapper can be held in a **GIA**. This makes it easy to monitor and review your investments, buy, sell and rebalance them and obtain instant valuations of your entire portfolio in one place. It also offers a way to easily manage cash through your platform, as well as acting as a holding pen for withdrawals or short-term funds. Some platforms also offer a range of fixed rate cash deposits through their GIAs, allowing a higher or more stable interest rate to be targeted.

GIAs do not directly benefit from any special tax reliefs or exemptions, unlike pensions, ISAs and investment bonds, so they are not technically 'tax wrappers'.

However, they are often referred to in this way because they look just like a tax wrapper on the platform, grouping income and capital gains together for easier reporting.

You can also offset any available annual Income Tax and Capital Gains Tax allowances against any income or gains arising within a GIA.

The amount of tax you pay on your investment income and gains depends on how much other income and gains you receive each tax year. Dividends, for example, are added on top of any 'earned' income you receive (e.g. from employment or pensions) and taxed at whatever rate of Income Tax applies to that level of income.

- In addition to your main Personal Allowance (currently £12,570.00 per tax year per person), you can receive up to £500.00 of dividend income each tax year before you have to pay any Income Tax on it. This is called the Dividend Allowance.
- You can also receive up to £1,000.00 of savings interest each year (e.g. from your cash savings or from fixed interest payments arising on corporate bonds, gilts and fixed interest funds) before you have to pay any Income Tax. This is known as the Personal Savings Allowance. If you are a higher rate (40%) taxpayer, this allowance is reduced to £500.00. If you are an additional rate (45%) taxpayer, you do not receive this allowance at all.
- If your non-savings income (pension income, salary, rental income, etc.) does not exceed the £12,570.00 Personal Allowance, there is also a £5,000.00 pa Starting Rate Band that can be used to receive tax-free interest. This is reduced by £1.00 for every £1.00 of non-savings income that exceeds the Personal Allowance, so if you have pension or salary income, for example, of £17,570.00 gross, no Starting Rate Band would be available.
- Each tax year, you can bank gains on your investments (e.g. when you sell them, in part or in full) of up to £3,000.00 before you have to pay any Capital Gains Tax. Capital gains on investments above the allowance, are now taxed at 18% in the basic rate band when added to your income in the same tax year, and 24% in the higher or additional rate band.

The amount of Income Tax you pay each year depends on the total amount of income you receive, what type of income it is, and which tax band it falls into, as summarised below.

UK tax rates and bands 2026/27

Tax band	Range of income within tax band	Tax rate on band	
		Dividends	Other income[1]
Basic	£12,571.00 to £50,270.00	10.75%	20.00%
Higher	£50,271.00 to £125,140.00	35.75%	40.00%
Additional	Above £125,140.00	39.35%	45.00%

[1] Such as salary, savings interest, property income and pension income.

Scottish taxpayers are subject to different tax bands and rates for certain types of income, but they have the same rates and allowances as the rest of the UK for savings income and dividends.

From 6th April 2027, new Income Tax rates will be applied to savings and property income: 22%, 42% and 47% respectively.

INDIVIDUAL SAVINGS ACCOUNTS (ISAS)

ISAs are one of the most common tax wrappers, giving you specific tax benefits.

They are exempt from Income Tax and Capital Gains Tax, which means that any assets you hold inside them (whether cash, direct stocks and shares or collective funds) grow faster, as they do not suffer the drag of taxation on their interest, dividends and capital growth, and the income and gains generated do not count towards the owner's total taxable income. Any money withdrawn from them is also free from Income Tax and Capital Gains Tax.

As with all investment wrappers that provide tax benefits, there is a limit to the amount you can pay in. For the current tax year, the maximum that you can invest into a new ISA is **£20,000.00** per person.

If you have a 'flexible ISA', however, any money withdrawn from the ISA (including certain fees) can be paid back into the ISA in the same tax year without using any of that tax year's ISA allowance.

ISAs are not generally exempt from Inheritance Tax, so they normally form part of your taxable estate when you die, which means they cannot be truly described as being 'tax-free'. However, it is possible to invest in certain assets through ISAs (Alternative Investment Market (AIM) shares) that potentially qualify them for a reduced rate of Inheritance Tax.

When you die, a spouse can inherit your ISA funds (known as an 'Additional Permitted Subscription'), so they continue to benefit from the tax efficiency of your ISA cash or investments. However, when the surviving spouse subsequently dies, the ISA wrapper is dissolved and the assets become unwrapped – i.e. they go back to being a taxable Unit Trust/OEIC/GIA.

CASH ISAS AND STOCKS AND SHARES ISAS

There are a few different types of ISA available. The main ISAs, as described above, are purely available for adults and are used as tax wrappers that you place investments into. They are called **stocks and shares ISAs**. However, you can also hold cash savings accounts within an ISA, known as a **cash ISA**. The annual subscription limit is currently exactly the same as for a stocks and shares ISA.

All interest received from a cash ISA is paid free from Income Tax. There is no Capital Gains Tax to pay on a cash ISA either, although cash savings are exempt from Capital Gains Tax in any case. This means that cash ISAs could be viewed as being less tax efficient than stocks and shares ISAs. It is generally good practice to use ISAs for assets that are likely to grow the fastest or that would normally suffer the most tax, so stocks and shares ISAs offer the maximum benefit from the ISA wrapper's efficiency.

It is possible to invest in multiple ISAs across both stocks and shares and cash within a single tax year, provided the total subscriptions are within your annual ISA allowance. However, from 6th April 2027, it will only be possible to place up to £12,000.00 per tax year of the total £20,000.00 ISA allowance into a cash ISA, unless you are over 65.

JUNIOR ISAS (JISAS)

JISAs are ISAs specifically for children. The annual allowance for JISAs is lower than for adult ISAs, at **£9,000.00** per child, per year, in the current tax year. JISAs benefit from the same tax exemptions as adult ISAs and they can also invest in cash, stocks and shares or a combination of the two across multiple arrangements.

The child is not permitted to have access to the JISA capital until they reach 18, however from age 16 they can decide for themselves how their JISA is invested if they wish.

At age 18, the JISA is normally converted into a full adult ISA and the subscription limit increases to the standard ISA allowance of £20,000.00 per tax year. Some JISA providers may require the investor to transfer their JISA to an alternative product or provider at that time for the funds to continue as an adult ISA.

It is important to note that once money is paid into a JISA, it is considered to belong to the child owning the JISA. That means they can access it as they wish, and use it however they choose, from age 18. The person who set up the JISA will have no control over this.

LIFETIME ISAS (LISAS)

LISAs are available to young adults aged 18 to 39. They are designed specifically to incentivise people to save for a first home, retirement, or both. The annual subscription limit for a LISA is up to **£4,000.00** per tax year. However, the Government will add a bonus of 25% to the value of any subscriptions paid into the LISA each year. For example, if you invested **£4,000.00** into a LISA this year, the Government would add a further **£1,000.00** (25%) to your investment, so that **£5,000.00** would actually be credited.

As with other types of ISA, LISAs can invest in cash, stocks and shares or both. However, as a general rule, cash or lower risk investments are more suitable for short- to medium-term goals and higher risk investments are more suited to longer-term goals, as cash is unlikely to keep up with the rate of inflation.

LISAs come with a number of restrictions on how and when the investor can access the LISA without the Government applying a withdrawal penalty. These include the following although this is not an exhaustive list:

- If you are using the fund to buy a home, you must never have owned a property anywhere in the world before. You must be a genuine first-time buyer.
- The property you are buying must be worth £450,000.00 or less and you must be using a mortgage towards the cost of it.
- You must not buy the property specifically to rent it out.
- You must be using a solicitor or conveyancer to act for you in the purchase, and the LISA funds will be paid to them for the purchase.
- You need to have the LISA open for at least a year before you access it.
- You can only pay into it up to age 50.

- If you are using the LISA for retirement rather than to buy your first property, you need to be at least 60 years old to access it without a penalty. In most instances, a pension would be more tax efficient and flexible than a LISA for retirement planning purposes, depending on your personal Income Tax rate, and when you plan to retire.

Any subscriptions made to a LISA will use part of your standard annual ISA allowance of **£20,000.00** per tax year. However, only the amount you contribute personally (i.e. up to **£4,000.00** into the LISA) will count towards your **£20,000.00** overall subscription. The Government bonus of up to **£1,000.00** per year does not count towards the **£20,000.00** subscription limit. For all types of ISA, the subscription limits are per person, per tax year.

It is important to understand that if a withdrawal penalty is applied due to money being taken from the LISA before age 60, where this is not for a qualifying first home purchase, this penalty is not simply a clawback of the bonus added, but rather 25% of the value withdrawn, which *will include the bonus and part of the money paid in*.

For example, if you paid in £4,000.00 and received a £1,000.00 Government bonus, and then withdrew the combined £5,000.00 in a non-qualifying way, the Government would charge a penalty of 25% of £5,000.00, which would be £1,250.00. This means that £250.00 of your own money is lost, as well as the full Government bonus.

LISAs are potentially going to be reformed in the near future, with the Government considering delaying the point at which the bonus is added to when a property is purchased, meaning that no growth can be achieved on that bonus, and there would no longer be any real advantage in using them for retirement planning.

INVESTMENT BONDS

Investment bonds come in two forms: **'onshore bonds'** and **'offshore bonds'.** Onshore bonds are registered in the UK for tax purposes, whereas offshore bonds are normally registered overseas, such as Dublin, Luxembourg, the Isle of Man or the Channel Islands.

Investment bonds are technically known as 'single premium life insurance' policies. However, they are really investment products that include a nominal amount of life insurance – typically 0.01% to 1.00% of the value held. They are not really suitable for traditional life assurance purposes, such as paying off a mortgage when you die, unless your plan is to repay debts from capital.

The phrase 'single premium' relates to the amount that you invest as a lump sum. Normally, life insurance is funded by monthly payments called 'premiums'. However, investment bonds are designed to be funded by a one-off investment lump sum, which you can normally add to at a later date. They can usually be set-up with recurring payments instead, but that is not their ideal purpose or structure, considering the tax complications this would introduce.

The life assurance company offering the investment bond will invest your single premium on your behalf in the underlying collective investment funds (or life funds, for some investment bonds) you have chosen, which should build up over time until you withdraw money from your policy.

Importantly, investment bonds are completely different from fixed interest 'bond' investments, such as corporate bonds and Government gilts. An investment bond is a tax wrapper that can potentially hold these types of assets, rather than being a fixed interest asset itself. They also differ from 'bond' cash savings accounts, and Premium Bonds.

One of the main benefits of investment bonds is that you can withdraw up to 5% of the premium(s) paid into it each policy year, without paying any immediate tax. This is known as the **5% tax deferred withdrawal allowance**. These withdrawals are deemed to be a return of capital, rather than 'income'. This allowance is available to both onshore and offshore bonds, but it has to build up before you can withdraw it, and it is capped at 100% of the total premiums paid (after 20 years).

ONSHORE BONDS

Onshore (UK-based) investment bonds are classed by HMRC as 'non-income producing' tax wrappers. They are taxed differently to other UK-based investments, which can provide valuable tax planning opportunities.

The investments you hold within an onshore bond are subject to UK life fund taxation, which is taken care of within the bond, and you are treated as having paid basic rate (20%) Income Tax on the income and growth achieved as a result. This notional tax is not repayable in any circumstances. However, the tax credit can be set against any further gains that are achieved along the way, which normally allows basic rate taxpayers to encash their onshore bonds without any further tax liabilities.

Certain events, known as **chargeable events**, can occur during the lifetime of your onshore investment bond. If a chargeable event is triggered and the bond has made a profit – a **chargeable gain** – there may be an Income Tax liability.

These chargeable events include:

- Death (of the last 'life assured')
- The maturity of the bond (for Capital Redemption bonds)
- Cashing in all of your bond or individual policies ('segments') within it
- Withdrawing more than the available tax deferred withdrawal allowance
- Assigning the bond (or its segments) to someone else for money (or money's worth)

As you are treated as having paid basic rate tax on the gain, the maximum tax rate you should be liable for is the difference between the basic rate and higher or additional rates of tax, depending on your total income from all sources in the tax year in which the chargeable gain arises. Broadly speaking, if the chargeable gain realised is within your Personal Allowance or basic rate tax band, there should be no further tax to pay. There should only be tax to pay if the gain takes your income into the higher or additional rate tax band.

For example, if a chargeable gain makes you a higher rate taxpayer, you may need to pay up to **20%** Income Tax on your gain (i.e. **40%** higher rate tax, less the **20%** notional tax that has already been paid within the bond). However, this views the calculation in very simplistic terms, as the interaction of bond gains with your other income, factoring in 'top-slicing relief', makes it quite complicated in reality.

Chargeable gains may also affect your eligibility for certain tax credits, and you could lose some or all of your entitlement to the Personal Allowance or Personal Savings Allowance.

Please also note that Scottish taxpayers are subject to UK tax rates and allowances on investment bonds (onshore and offshore) even if the banding and tax rates on their other income differ from those mentioned above.

OFFSHORE INVESTMENT BONDS

Offshore investment bonds are similar to UK investment bonds, as chargeable events occur on the same events described above for onshore bonds. The main difference is in how any chargeable gains are taxed.

The income and growth inside an offshore bond do not suffer UK life company taxation along the way (i.e. Corporation Tax). Instead, offshore bonds are allowed to grow virtually tax-free, with the exception of a small amount of Withholding Tax (if any) that may be deducted from interest and dividends received by the funds in the offshore jurisdiction the bond is held in. This means that offshore bonds can potentially grow faster than onshore bonds, especially over the very long-term.

The main drawback is that, when a chargeable event occurs, you will pay Income Tax on the gain at your **highest** marginal tax rate, with no basic rate tax credit.

To simply compare the two bonds, with an onshore bond, you pay broadly the equivalent of basic rate tax on your bond throughout its lifetime, but receive a credit for the basic rate tax when a chargeable event arises, whereas with an offshore bond, you pay virtually no tax on the investment during its lifetime, but you may pay a higher level of tax on chargeable events when they arise.

Again, offshore bond gains may affect your eligibility for certain tax credits and you could lose some or all of your entitlement to the Personal Allowance or Personal Savings Allowance.

That said, for people with lower incomes, offshore bonds can be very efficient, as their gains are treated as savings income. That means any available Personal Allowance, Starting Rate Band or Personal Savings Allowance can potentially be offset against offshore bond gains, making them tax-free, or reducing the overall tax payable. Depending on the investment timeframe and the owner's tax position, an offshore bond could be more tax efficient overall, even if there is some tax to physically pay on encashment.

TOP SLICING RELIEF ON CHARGEABLE EVENT GAINS

Top slicing relief may reduce the amount of tax payable on chargeable gains – both for onshore and offshore bonds. It is usually available where the bond owner would be liable to tax at a lower rate were it not for the inclusion of the chargeable gain (for example, you are normally a basic rate taxpayer but the chargeable event gain pushes you into the higher rate tax bracket). It may reduce the tax payable on a bond gain, but it does not reduce the gain itself.

Very simply, top slicing relief aims to spread the gain achieved over the number of complete policy years that the bond has been held, to reduce the tax payable on the gain being realised all at once. However, the process for calculating it is complicated and the full gain is always used to calculate how much Personal Allowance and Personal Savings Allowance is available.

For some offshore investors, 'time apportionment relief' may also help to reduce any tax payable, although this only applies to people who have lived overseas while holding their bond, so we have not covered it in any detail here.

TAKING WITHDRAWALS FROM THE BOND

As previously noted, you can withdraw up to 5% each year of the premium you invested into your bond without paying any immediate tax on it – i.e. the 5% tax deferred withdrawal allowance. This allowance is cumulative, so any unused part of this 5% limit can be carried forward to future years.

The maximum you can withdraw within this 5% tax deferred limit is 100% of the amount paid in. For example, you could withdraw 5% each year for 20 years, or 4% each year for 25 years, and so on.

However, if you decide to take more than the accumulated 5% tax deferred allowance, you will create a gain equal to the amount that exceeds your available allowance.

The life company will send you details of the chargeable event gain arising for you to notify HMRC, and you may be subject to Income Tax. Care must be taken, as some fees and charges use up part of the tax deferred allowance, as well as counting towards any chargeable gains that may arise.

INVESTMENT OPTIONS

Traditionally, offshore bonds have tended to offer more investment options than onshore bonds. However, many onshore bond providers – particularly those available through wrap accounts – now offer access to hundreds and sometimes thousands of different funds.

As investment bonds are, strictly speaking, exempt from Capital Gains Tax, you can switch between the funds within them without a tax liability. This makes them ideal for investment strategies that are likely to require significant fund switching or dealing, such as portfolios managed by discretionary fund managers.

As the annual Capital Gains Tax allowance has gradually reduced in recent tax years, and as Capital Gains Tax rates have recently increased, onshore and offshore bonds may now be a more attractive option for people with larger amounts to invest, where this cannot be immediately placed in ISAs or pensions.

TAX AND ESTATE PLANNING

Investment bonds are useful for inter-generational tax planning – such as for holding substantial assets in trust, to be passed to your beneficiaries at a later date. It is also possible to assign all or part of an investment bond by way of a gift, and this could be especially tax efficient if the recipient pays a lower rate of tax than you. This makes them particularly attractive for Inheritance Tax planning.

PENSIONS

Until recently, pensions have generally been considered the most tax efficient wrapper available. For this reason, the rules regarding what you can pay into them and when you can access them are more restrictive than for other tax wrappers.

Pensions have always been attractive for very long-term investments, such as meeting your retirement needs. This will still be the case once they become subject to Inheritance Tax from 6th April 2027, but they are no longer *as* useful for flexible legacy planning as they once were.

Pension legislation has evolved significantly over the years and there are now many different types of pensions available to investors. It is not uncommon for someone to accumulate several different pension arrangements over their lifetime, for example through different employments.

Each type of pension will have its own individual structure and/or set of rules and limitations. These typically relate to:

- How much you can pay in
- How you can draw benefits
- How and where you can invest the money inside it
- How any benefits are treated and/or passed to your beneficiaries when you die
- The charges applicable, and whether there is any limit to those charges
- Whether you can lend to, or borrow money from, them
- Whether the benefits accrued within your pension are secure/guaranteed or not

There are two main types of pension: **occupational pensions** and **individual pensions**.

OCCUPATIONAL PENSIONS

Occupational pensions are set up by, and usually paid for by, an employer on behalf of its employees. There are two sub-types of occupational pensions, which are:

- **Final salary (also known as 'defined benefit') schemes** – whereby you accrue an entitlement to a known, secure pension income when you retire, based on your salary and years of service with the employer. Normally, you do not personally bear any investment risks or charges; the retirement benefits are promised to you by the employer, which invests the assets within the pension scheme on behalf of its members. If the assets within the pension scheme do not grow sufficiently for the employer to meet its liabilities when its members retire, the employer will be expected to add further capital to the pension scheme to address any shortfall.

  These are normally regarded as the most valuable and secure type of pension, but this depends on the solvency of the employer to a large extent.

- **Money purchase (also known as 'defined contribution') schemes** – whereby the scheme is owned and operated by the employer (normally via a life company, which provides the administration of the scheme), but there is usually no promise of a secure future benefit.

  The value of your pension – and what it will provide in retirement – is dependent on how and where your benefits in the scheme are invested. You make the investment decisions yourself. The individual members of these schemes usually bear little or no costs, although they might need to pay a small charge for the funds they choose to invest in.

  Money purchase schemes are very commonly used, whereas final salary schemes are becoming increasingly rarer, given the significant costs and risks to employers of operating them. Hence, final salary schemes are generally considered to be 'gilt-edged' pensions, because they offer significant value and benefit to employees in retirement.

Some occupational money purchase schemes, usually older ones, offer some hybrid benefits, such as Guaranteed Minimum Pensions (GMPs) or protected tax-free cash, so existing occupational schemes should always be handled with care.

INDIVIDUAL PENSIONS

Individual (or personal) pensions are usually money purchase schemes. The value of your pension fund will depend on how much you (or your employer or another third party) pay into it and the growth achieved by any investments or assets that you hold inside it.

Most modern pensions operated by employers are individual pensions, rather than occupational pension schemes. Examples of employer-related individual pensions are:

- Group Personal Pensions
- Group Stakeholder Pensions
- Qualifying Workplace Pensions (i.e. auto enrolment schemes)

These are different to traditional occupational pensions because the individual members normally bear all the charges and have to make investment choices themselves. They may also have greater control over how and when any benefits are paid to them. However, being part of a larger group scheme often means that the employer can negotiate a discount in the charges that you would normally pay, and these can sometimes be quite substantial.

TAXATION

Pensions are still one of the most tax efficient wrappers available, but their tax reliefs are about to become less generous. They are given significant tax incentives to encourage people to make their own provision for retirement, reducing their reliance on the State Pension and enabling us to live more than a subsistence lifestyle when we stop working.

However, the introduction of flexible withdrawal options and very efficient death benefit treatment, coupled with the abolition of the Lifetime Allowance, has resulted in them being considered *too generous*, particularly for the very wealthy, making them a target for tax rises.

Pensions have increasingly become seen as a way of passing on money free from Inheritance Tax, while still giving the investor access to this money in lifetime if it is needed. The current Labour Government has therefore announced that pension funds will no longer be exempt from Inheritance Tax on a person's death (aside from when left to a spouse or civil partner) from 6th April 2027. This will mean more Inheritance Tax is payable for many, but pensions are still a very tax efficient way of building money for retirement, considering the other tax reliefs on offer, and spending them will become more attractive when the incentives for keeping them as a legacy have diminished.

When we talk about pension contributions, we normally refer to them as being either 'gross' or 'net'. A 'net' contribution is the amount that you physically pay from your bank account or after-tax salary. A 'gross' contribution is the amount that is invested into your pension fund by the pension provider on your behalf, after tax relief has been added.

Tax relief on contributions

When you pay a personal contribution into a pension fund, it will normally attract basic rate tax relief (which is currently at 20% in the UK) This means that, for every net contribution of £80.00 that you pay into your pension, a total of £100.00 gross will be credited to it.

The additional £20.00 (i.e. 20% of your gross contribution of £100.00) is reclaimed from HMRC by your pension provider and added to your fund.

- If you are a higher or additional rate taxpayer by virtue of your other income that tax year, you can claim even more tax relief on top of this via your Self-Assessment Tax Return. For example, if you are normally a higher rate taxpayer (i.e. you pay 40% tax, you can claim a further 20% of tax relief on top).
- For additional rate taxpayers, you can claim up to 25% via Self-Assessment. This higher/additional rate tax relief is not added to your pension fund, though. Instead, it is applied as an extension to your basic rate tax band. This means that, for that tax year, you will pay Income Tax at 20% on more of your income, and at 40% or 45% on less.
- For very high earners, pensions may even allow all or part of the Personal Allowance to be reclaimed, where this is lost due to their income exceeding £100,000.00 gross in a tax year. Care must be taken with the available Annual Allowance, however, as this is 'tapered' for those with higher incomes. This is covered in more detail later.
- Scottish taxpayers can also receive tax relief on pension contributions, based on the Scottish Income Tax rates and allowances (the figures above are based on the UK position).

Taxation of the underlying assets and investments within the pension

While your pension fund has not yet been drawn upon (i.e. it is '**uncrystallised**'), the assets inside it are permitted to grow free from Income Tax and Capital Gains Tax. This means the funds will grow more quickly than they would in wrappers that are taxed on an ongoing basis, plus personal contributions have the benefit of the initial tax relief uplift.

When you draw benefits from your pension fund (known as '**crystallising**' it), you can normally take up to 25% tax-free. This is known as a '**Pension Commencement Lump Sum (PCLS)**', or more commonly, '**tax-free cash**'. The other 75% of your fund will be subject to Income Tax when withdrawn.
The rate of Income Tax you pay depends on your total income that tax year, so it works in a similar way as income from employment or self-employment (although no National Insurance Contributions are due).

You will therefore either pay no, basic rate, higher rate or additional rate tax (or the applicable Scottish rates), depending on how much of the fund you withdraw (when it is added to your income from any other sources) that year.

It is possible to only crystallise part of your pension fund and leave the rest uncrystallised. In other words, you can draw only what you need, when you need it. This is called 'phased retirement'. Where this strategy is used, the same tax position above applies. Therefore, you only pay Income Tax when you draw taxable income from your pension fund, above any tax-free lump sum. Alternatively, you can use all part of the fund to buy a lifetime or fixed term annuity, with a regular taxable income stream being secured by an annuity provider.

Pension funds are normally exempt from Inheritance Tax when you die – irrespective of whether that is before or after you draw any benefits. This is due to change from 6th April 2027, however, and Income Tax is payable on death benefits passed on if the owner is aged 75 or over on death.

You should bear in mind that any income or tax-free cash withdrawn from your pension fund in the 2026/27 tax year is likely to form part of your potentially taxable estate for Inheritance Tax purposes unless you spend it, while it would remain free from Inheritance Tax inside the pension until 6th April 2027. It is therefore generally advisable to only draw money out of your pension before then if you are likely to spend it in the short-term, or if it can be given away within an Inheritance Tax gifting exemption.

ANNUAL ALLOWANCE, LUMP SUM ALLOWANCE AND LUMP SUM AND DEATH BENEFIT ALLOWANCE

As with all tax reliefs and allowances, there are limits for pensions.

Annual Allowance and tax relief

The Annual Allowance is the maximum you (and anyone else on your behalf) can contribute to a pension each year before there would be an Annual Allowance tax charge.

Each person's Annual Allowance depends on their earnings, how much they have already paid into a pension that tax year, and the legislation that applies at the time.

There is also a separate test to determine the maximum personal contribution that can be made each tax year with full tax relief being available. In most cases:

- There is a basic **Annual Allowance of £60,000.00 gross** for the current tax year.
- However, the maximum personal contribution that can be made with full tax relief being available is capped at the higher of 100% of your net relevant earnings (e.g. salary from employment or self-employment), or **£3,600.00** gross (**£2,880.00** net of basic rate tax relief) for people with lower or no earnings. Personal contributions include any pension payments made as 'employee contributions', although the contribution limits on defined benefit schemes are more complicated.

This means that, even if you are not working and have no income, you can still contribute up to **£3,600.00** gross (**£2,880.00** net) into a pension either personally, or on behalf of someone with no earnings. The pension-holder would still benefit from basic rate tax relief. Tax relief on pension contributions is only available up to age 75.

If you exceed the Annual Allowance, you will pay tax on any excess contributions at your personal marginal rate that tax year. If you exceed the maximum tax relieved contribution, you would not receive tax relief on the full contribution paid.

It is possible, in some circumstances, to **carry forward** any unused reliefs from up to three previous tax years in addition to the current tax year. The rules regarding this are quite complex and – for contributions paid personally rather than by an employer – you would need to have sufficient net relevant earnings for the full tax reliefs to be granted. However, it is a useful way for higher earners to boost their pension savings.

Tax relief on employer contributions is subject to a different test, as these are normally paid gross and give your employer Corporation Tax relief (if considered 'wholly and exclusively for the purposes of a trade') rather than giving you Income Tax relief. Employer contributions therefore are not capped at your salary, but they do have to be reasonable as part of your overall remuneration package, considering your role in the business.

Annual planning with employer pension contributions is most powerful for people who run their own companies, however, many employers offer 'salary sacrifice', which allows you to exchange some salary for a higher employer contribution, directly reducing your ongoing Income Tax and National Insurance Contributions. The November 2025 Budget announced a proposal to apply a £2,000.00 per tax year limit on salary sacrifice contributions from 6th April 2029, which would significantly narrow this tax planning opportunity thereafter if it comes to pass.

Any tax relief granted on employer contributions is subject to HMRC approval, and it is not a cut and dried test, so it is usually advisable to take advice from the company's accountant before making any large employer contributions.

The Annual Allowance is tapered away for the highest earners. Those with 'adjusted income' exceeding **£260,000.00** and 'threshold income' exceeding **£200,000.00** will have their Annual Allowances reduced by £1.00 for every £2.00 that their income exceeds **£260,000.00**. The minimum Annual Allowance available to individuals that this applies to is **£10,000.00** gross per year. This is quite a complicated calculation, and employer contributions themselves can reduce the Tapered Annual Allowance available.

Lifetime Allowance and Lump Sum Allowances

For many years, there was also a limit on the amount of pension capital you could accumulate during your lifetime without an additional tax charge. This was known as the Lifetime Allowance, but it was abolished in the 2023/2024 tax year, at which point the limit stood at £1,073,100.00 for most people.

This means there are no longer any Lifetime Allowance tax charges on pension funds if this allowance is exceeded. However, two main lump sum allowances have been introduced in its place, which may be an issue for people with larger pension funds, or valuable defined benefits.

- All tax-free lump sums, including tax-free lump sum death benefits, are now tested against a lifetime limit, currently set at £1,073,100.00. This is known as the **Lump Sum and Death Benefit Allowance (LSDBA)**.

  Any lump sums paid above this level will be taxed at the individual's or beneficiaries' marginal rate of Income Tax. If paid to a Trust, they will generally be taxed at basic rate Income Tax, unless paid outside of the two-year period, or when the deceased was over 75 on their death, when they will be taxed at 45%, with the potential for beneficiaries to claim a tax credit against their withdrawals if they pay tax at a lower rate.
- Within that overall limit, there is a cap on the total lump sum that can be taken tax-free during lifetime. For most people, this refers to their tax-free cash (or Pension Commencement Lump Sum), including the tax-free element of Uncrystallised Funds Pension Lump Sums. This tax-free limit is known as the **Lump Sum Allowance (LSA)**, and it is currently set at £268,275.00 (which is equivalent to 25% of £1,073,100.00).

There is also an Overseas Transfer Allowance of £1,073,100.00, but this will not apply to most UK residents unless they have lived abroad and hold overseas pension schemes, or are planning to emigrate and want to take their pensions overseas too.

Anyone with a Lifetime Allowance 'protection' certificate (for example Fixed Protection or Individual Protection) may be entitled to a higher LSA and LSDBA. Any pension-holders that have previously been entitled to a higher level of tax-free lump sum will also retain that right. This could be because they were entitled to a higher level of Lifetime Allowance resulting in a higher level of tax-free cash or because they have scheme specific lump sum protection.

Where the above rule changes mean that previous benefits are miscalculated when determining how much LSA and LSDBA remain, it is possible to apply for a Transitional Tax-Free Amount Certificate (TTFAC) to amend the calculation and potentially increase the remaining allowances. For example, where a defined benefit pension was taken in the past without any tax-free cash being claimed, the standard calculation would assume 25% of the total benefits crystallised had already used LSA and LSDBA, when in actual fact no LSA or LSDBA had been used at all, as no lump sums had been taken.

The lump sums that are tested against the *Lump Sum and Death Benefit Allowance* include:

- Pension Commencement Lump Sums and the tax-free elements of any Uncrystallised Fund Pension Lump Sums
- Uncrystallised Funds Pension Lump Sum death benefits
- Drawdown pension fund lump sum death benefits and Flexi-Access Drawdown lump sum death benefits
- Stand-alone lump sums
- Serious Ill-Health Lump Sums
- Defined benefit lump sum death benefits
- Pension protection lump sum death benefits
- Annuity protection lump sum death benefits

MINIMUM PENSION AGE

You can normally take benefits from your pension at any time from age 55. There is no upper age limit, although some pension providers require you to take benefits or move your pension to another policy by age 75. If you choose to leave your pension funds invested for the rest of your life, you can.

With effect from 6th April 2028, the minimum pension age will increase from 55 to 57, linking it to 10 years below each person's State Pension Age (which rises to 67 from 2028). There are transitional rules for people who turn 55 before 6th April 2028 but who are still under 57 at that date, whereby there is a window of time to take benefits before 6th April 2028, otherwise no access is allowed until age 57.

The minimum pension age is rumoured to be increasing again in the future, likely to at least 58 for those with a State Pension Age of 68, so every time the State Pension Age increases, the minimum pension age will probably also increase. This is because the population is increasingly living longer, so our pension funds also need to last longer. It is for this reason that we will often consider alternative tax wrappers – not just pensions alone – for meeting retirement objectives.

Currently, members of 'uniformed pension schemes' (including the armed forces, police and fire services) will be exempt from the new rules, and many of these pension schemes may have an even lower protected pension age.

There are also some pension schemes that were written 'to age 55' rather than 'to normal minimum pension age' that may still allow access at 55, but, in reality, few people have a need or desire to take pension benefits this early.

DRAWING BENEFITS

There are three main ways that you can draw benefits out of a pension:

- A secure pension income, or 'annuity'
- Uncrystallised Fund Pension Lump Sums (UFPLS)

- Flexi-Access Drawdown (FAD)

Our Pension Income Options Guide outlines these in detail. Please ask as for a copy if you would like to see it.

Not all types of pension – or pension providers – offer all these options. It may be necessary to transfer your pension funds to an alternative provider to access the most flexible retirement options.

DEATH BENEFITS

If you die before reaching age 75, your pension funds will, currently, normally be passed to your beneficiaries completely tax-free.

If you are over 75 when you die, your beneficiaries will pay Income Tax on the benefits at their own marginal tax rates, depending on their other income in the year of the withdrawal. This is the case irrespective of whether or not you have taken all the tax-free cash available to you; tax-free cash can only be taken in your lifetime.

These death benefits are subject to the Lump Sum and Death Benefit Allowance discussed above, if they are taken as a lump sum rather than as an inherited pension fund. This is only really an issue on death before age 75, if the benefits are taken as a lump sum, and that lump sum exceeds the Lump Sum and Death Benefit Allowance (currently £1,073,100.00 reduced by any allowance that has already been used). A tax charge on the excess can be avoided by taking the benefits as an income instead, which includes using it as a beneficiaries' FAD pension.

Your beneficiaries will have the same benefit withdrawal options as you, including buying an annuity, or taking FAD withdrawals, although UFPLS will not be possible due to there being no entitlement to tax-free cash. They can also leave their inherited pension fund invested, as a pension, for as long as they like, growing free from Income Tax and Capital Gains Tax. However, this assumes the pension you left offers FAD, or at least the option to transfer the inherited fund to another provider that does offer these withdrawal options.

When you die, the beneficiary of your pension fund is known as a 'nominee' (spouses and civil partners may instead been called 'dependants'). It is possible for the nominee/dependant to leave any of their inherited pension fund to their own beneficiaries, who are known as 'successors'. In this way, a pension fund can be passed down through several generations. If you were under 75 at the time of your death, the pension fund will continue to be available, tax-free, to your nominee and any further successors, until it has been exhausted. However, the tax treatment would change if the nominee, dependant or successor passing it on after their death was over 75 when they passed away. The tax treatment is based on the age at death of the person who directly passes their pension fund to you.

The tax treatment above will still apply to pension death benefits from 6th April 2027, but this will be applied to the pension fund that remains after any Inheritance Tax payable has been deducted.

ESOTERIC INVESTMENTS

VENTURE CAPITAL TRUSTS (VCTS), ENTERPRISE INVESTMENT SCHEMES (EISS), SEED EISS & BUSINESS RELIEF SCHEMES

These are often collectively known as 'esoteric investments', as they are not mainstream tax wrappers and are only suitable for investors with very specific needs and circumstances.

They are all ways for small, largely unquoted UK companies to raise money for growth and development. They are portfolios that hold single company shares in companies that have not yet floated on a main stock-exchange. They invest in small businesses looking for venture capital from investors who are willing to take higher risks with their money, in return for the possibility of higher returns, if the companies take off and eventually float on the stock-market, or are sold.

Historic Governments have been keen to encourage private investment in fledgling and smaller companies to drive the economy. To incentivise investors into this market (which is regarded as higher risk due to the increased chance of a smaller, or newer, company failing when compared with a large and established company listed on the FTSE All Share Index, for example), VCTs and EISs were established several years ago as a means for the public to invest in this market easily, and with significant tax advantages available. There is a sub-type of EIS, called a Seed Enterprise Investment Scheme (SEIS), which is specifically for the smallest and youngest businesses. Therefore, SEISs offer the highest Income Tax benefits.

Business Relief schemes are designed specifically for Inheritance Tax (IHT) planning, and afford different tax reliefs to VCTs and EISs/SEISs.

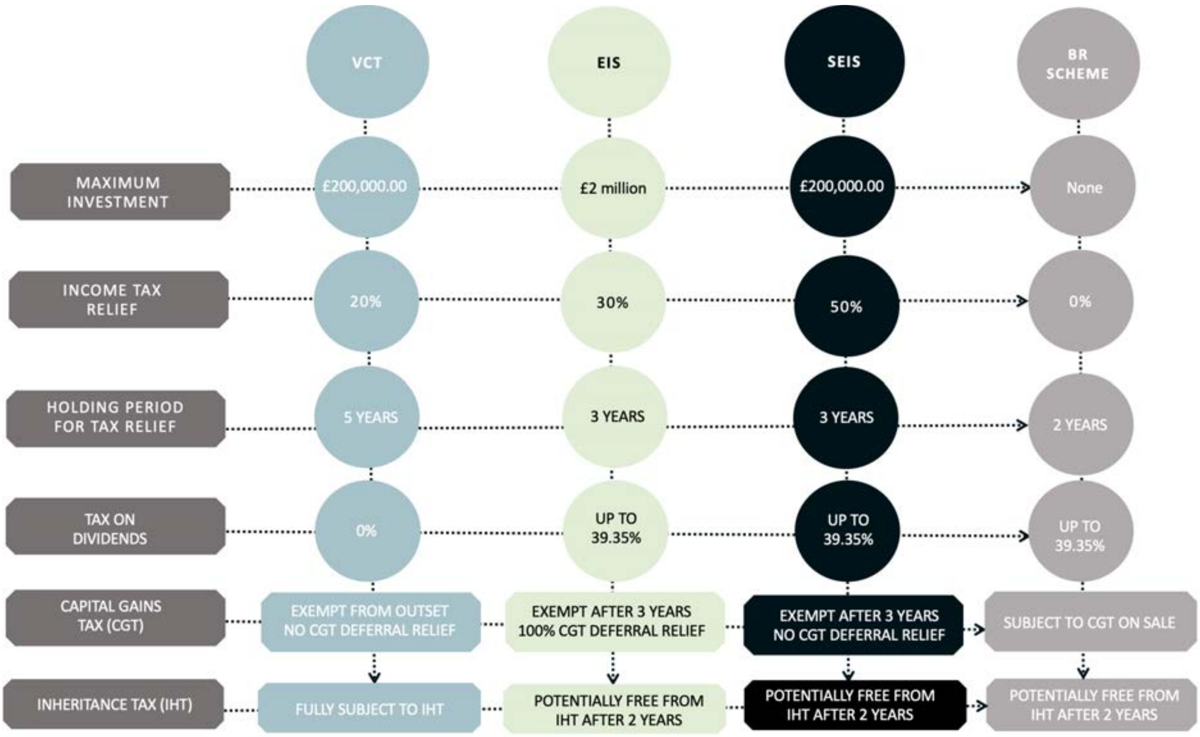
Some Business Relief targeting investments use companies listed on the Alternative Investment Market (AIM). However, as of 6th April 2026, Business Relief schemes that use qualifying AIM investments now only qualify for 50% Business Relief, meaning they will be taxed at 20% IHT rather than 0% as they have been historically. This is still a saving compared to the full 40% IHT rate, but this will make truly unquoted Business Relief schemes more attractive going forward. Business Relief on unquoted shares has also been limited from 6th April 2026, with the full relief being applied to the first £1 million held, and 50% relief (20% IHT) applying to the value above £1 million.

Most trades qualify for entry into esoteric investment portfolios, but some – which are termed 'excluded activities' – do not. For example, dealing in land or commodities, financial activities and property development are all excluded activities. A company can carry on some excluded activities, but these must not be 'substantial', which HMRC takes to mean as more than 20% of the company's activities.

Due to the significant tax benefits potentially available to these types of investments, investors are required to hold them for a minimum period before they can claim all the reliefs available, and avoid any of the initial reliefs being clawed back. The holding periods are a minimum of five years for VCTs and three years for EIS and SEIS investments. Business Relief investments have to be held for at least two years and still be retained on death to provide an IHT saving.

This prolongs the amount of time that an investor places their investment at risk, and relies on the companies held within the portfolio to continue trading for that long, and to remain 'qualifying' (i.e. unquoted and within the level of gross assets and staffing levels required by legislation).

Although very similar in purpose, VCTs, EISs, SEISs and Business Relief schemes offer different tax treatments for investors, which is best illustrated as a direct comparison, shown below.



VENTURE CAPITAL TRUSTS (VCTS)

The UK is one of the world's most successful markets for entrepreneurial small companies. However, companies that start small usually need investment capital to help them grow and develop.

Recognising that investing in smaller, unquoted companies involves taking more risk than investing in larger listed companies (for example, BP or Vodafone), the Government introduced VCTs in 1995 as a way of encouraging investment into Britain's exciting, entrepreneurial businesses. In the three decades since they were introduced, VCTs have helped to create jobs, reward innovation and bolster the UK economy.

Some companies that started off with funding from VCTs have grown to become household names in their own right, some have achieved a listing on the London Stock Exchange and some have been sold to global brands, such as Microsoft, Amazon and (as it was at the time) Twitter.

As well as providing investors with an easy way to access these small, unlisted or AIM-listed companies, VCTs offer a number of tax reliefs.

These tax reliefs have just been reduced, however the cap on the value of the assets held by a VCT has been increased at the same time.

VCTs now only offer 20% upfront Income Tax relief (30% to 5th April 2026), but any dividends paid from them are still tax-free and there should be no Capital Gains Tax to pay on any increase in the value of VCT shares sold once the required holding period has been reached.

It is important to understand that smaller companies can struggle in their early years, and some will not be successful. Therefore, the tax incentives are there to help compensate investors for the risk they take with their money.

ENTERPRISE INVESTMENT SCHEMES (EISS)

Launched in 1994, EISs also make investing in shares in early-stage businesses even more attractive, but they offer different tax incentives than VCTs.

When an early-stage business is EIS-qualifying, you can claim a number of tax reliefs alongside your investment, including upfront Income Tax relief, tax-free capital gains, and loss relief on each investment that returns less than you put in.

SEISs were introduced in 2011 and, as noted earlier, they specifically concentrate on smaller and younger businesses than traditional EISs. Investors in SEISs are therefore at higher risk of experiencing capital losses, which is why their tax incentives are comparatively more generous.

Due to the type of companies held, EIS and SEIS shares may also benefit from Inheritance Tax relief as long as they have been held for at least two years at the owner's death, and provided the underlying shares qualify. The total 100% Business Relief available to an investor has been capped at £1 million since 6th April 2026, with 50% IHT relief applying above this.

BUSINESS RELIEF (BR) INHERITANCE TAX (IHT) SCHEMES

These schemes target IHT relief through qualifying for BR. Investments that qualify for BR can be passed on free from IHT on the death of the investor, provided the shares have been owned for at least two years at that time.

BR has come a long way since it was first introduced in the 1976 Finance Act. Then, its main aim was to ensure that after the death of the owner, a family-owned business could survive as a trading entity, without having to be sold or broken up to pay an IHT liability. Over time, successive Governments recognised the value of encouraging people to invest in trading businesses regardless of whether they run the business themselves, however the current Labour Government has seen business and agriculture as an easy target for tax increases.

BR is a well-established relief dating back 40 years, however, you should keep in mind that the value of an investment may go down as well as up and investors may not get back what they originally put in. Tax rules may change in the future, and the value of tax reliefs depends on your individual circumstances.

Not every investment or interest in a business will qualify for BR, but BR will typically be available for:

- Shares in an unquoted qualifying company, even a minority holding (with a person's total 100% BR being capped at £1 million, with 50% relief above this).
- Shares in a qualifying company listed on the Alternative Investment Market (AIM) will attract a lower rate of BR – 50% – so they will be taxed at 20% rather than 0% or 40%).
- An unincorporated qualifying trading business, or an interest in one – a partnership, for example (the same IHT limits apply as for unquoted shares from 6th April 2026).

AIM-listed shares can be held through an ISA, sheltering them from Income Tax and Capital Gains Tax, but they no longer qualify for full BR.

One of the key benefits of BR schemes is the speed with which the capital can be relieved from IHT. Making gifts or settling assets into trust usually takes seven years to become completely free from IHT. Investments in a BR-qualifying company can be passed down to beneficiaries potentially free from IHT (or taxed at a lower rate of IHT) on the death of the shareholder, provided they have been held for at least two years at that time. Once a BR investment has been held for two years, it can potentially be given away free from IHT, but it must then be retained until the death of the donor to qualify for this beneficial tax treatment.

Owning BR-qualifying shares allows a client's wealth to stay in their own name, also giving them greater access and control compared with other IHT planning solutions.

BR-qualifying investments do not use the Nil Rate Band. This means investors can plan for their Nil Rate Band to reduce the IHT charge on less liquid assets, such as their home, which are otherwise difficult to place outside the estate for tax purposes. However, BR assets *do* count towards the £2 million threshold above which the Residence Nil Rate Band starts to be reduced, whereas lifetime gifts are ignored in this calculation, even if they are still inside the estate.

To qualify for these tax reliefs, a company must not be listed on a main stock exchange. Such companies could fall in value, and investors may get back less than they invest.

Investments in unquoted companies or those quoted on AIM can fall or rise more sharply than shares in larger companies listed on the main market of the London Stock Exchange, and may be harder to sell.

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The content of this document is for information only. It does not represent personal advice or a personal recommendation and should not be interpreted as such. Please do not act on any part of it without first having received individual independent financial advice.

The material is not intended as an offer or solicitation for the purchase or sale of any financial instrument.

The material is not intended to provide, and should not be relied on for, accounting, legal or tax advice, or investment recommendations.

Past performance is not a guide to future performance and may not be repeated.

The value of investments and the income from them may go down as well as up and investors may not get back the amounts originally invested.

The information is based on our understanding of current legislation. Tax rules could change in the future. The value of tax reliefs will depend on an investor's personal circumstances. There cannot be any guarantee that companies that qualify today will remain qualifying for the tax reliefs of these products in the future.

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