



Article

High Earner? Invest Tax-Efficiently Like This

Tax is one of those unavoidable facts of life. If you are a high earner, you will be well aware of this.

Many tax loopholes have closed over the past decade, but there are still numerous options for investing tax-efficiently.

Pensions

Pensions are one of the most tax-efficient investment options available. For example:

- Personal contributions receive 20% tax relief. So for every £80 you pay in, a further £20 is added by HMRC (providing your contributions do not exceed your relevant earnings).
- Higher and additional rate tax relief can be claimed through your tax return. An additional rate taxpayer may find that their £100 contribution costs as little as £55 out of net income.
- Contributions to an employer's pension can be even more efficient. If you contribute via salary sacrifice, your effective earnings are reduced, which means you could also save on National Insurance.
- Company contributions are generally an allowable expense for Corporation Tax purposes. This is subject to the agreement of the Local Inspector of Taxes.
- When your pension fund is invested, the income and growth are tax-free.
- You can withdraw 25% of your pension as a lump sum, provided you are over the minimum retirement age. The remaining pot can be drawn flexibly, taxed at your marginal rate.

However, there are some limits to the relief, which are particularly relevant for higher earners:

- Personal and employer contributions are capped at the level of the Annual Allowance. This is £60,000 per year. Exceeding this allowance not only results in paying the tax as if you received the money as income, but also means the money is tied up in your pension. It will then be taxed again when you begin drawing retirement benefits.
- However, if you have not fully used your Annual Allowance, you can carry it forward for up to three tax years, provided you were a member of a pension scheme throughout that period.
- Of course, this is subject to other limits. Personal contributions are still capped at the level of your relevant UK earnings. Company contributions must be considered reasonable, proportionate, and 'wholly and exclusively' for the purposes of trade.
- If you earn over £260,000, your Annual Allowance will be reduced. The rate of reduction is £1 for every £2 over the threshold.
- If you take a taxable income from your pension using flexible access (beyond your tax-free lump sum), your Annual Allowance will be reduced to £10,000 under the Money Purchase Annual Allowance (MPAA) rules. This also removes your ability to carry forward unused allowances from previous tax years.

ISAs

Once you have maximised your pension allowance, ISAs should be your next port of call.

- You can invest £20,000 per year into ISAs.
- All growth and income on the funds are tax-free.
- You can withdraw the money without tax or penalty.
- Any money withdrawn can be replaced in the same tax year without using up any of your ISA allowance.

- If you have other investments (such as shares or funds), you can gradually move investments into your ISA by selling them outside the ISA and repurchasing them within it, which may trigger Capital Gains Tax. This approach can help use your annual CGT exemption.

Of course, for a higher earner, £20,000 per year is relatively limited, and you may be looking for other investment options in addition.

Investment Bonds

Investment bonds (UK or offshore) can work well if you have a lump sum to invest. The advantages for a higher earner are:

- Income and gains generated within the fund do not form part of your personal tax calculation and do not need to be declared on your tax return.
- UK bonds pay some tax within the funds. Offshore bonds grow free of most taxes.
- You can withdraw up to 5% per year of your original investment without paying tax. Any unused allowance can be carried forward to future years.
- Bonds can be fully or partially gifted (to an individual or trust) without immediate tax liability.
- Tax only applies when the bond is encashed (fully or partially). So if you defer encashment until you retire, or gift the bond to someone else, it's possible that a lower tax rate will apply.

Venture Capital Trusts (VCT)

VCTs are a higher-risk investment option, but they can be suitable for higher earners. They allow you to invest in a selection of smaller companies with high growth potential. You can invest up to £200,000 in VCTs during the tax year. The tax advantages are:

- 30% tax relief on your investment.
- Dividends are free of tax.
- Gains are free of Capital Gains Tax.
- You need to hold the investment for at least five years to benefit from the relief.

Enterprise Investment Schemes (EIS)

An EIS works in a similar way to a VCT. However, it involves investing in just one company rather than several.

In reality, many investors hold portfolios of EIS investments, which can help to spread the risk. You can invest up to £1 million in EIS investments per tax year, although an increased limit of £2 million applies if you invest in knowledge-intensive companies.

An EIS offers the following tax benefits:

- 30% tax relief on your investment.
- You can apply the investment to a previous tax year, for example, if you had a higher level of earnings to offset.
- You can reinvest capital gains realised elsewhere to defer the tax.
- Gains on the EIS shares are free of Capital Gains Tax.
- You need to hold the investment for at least three years to benefit from the relief.

- Additionally, EIS investments typically qualify for Business Relief, which can provide some relief from IHT (the rules surrounding this are set to change in 2026).

Both EIS and VCT investments are extremely high risk and are not suitable for everyone.

While saving tax is an attractive proposition, remember, it is not a goal in itself. You should never make investment decisions solely due to tax efficiency, particularly if this involves taking higher levels of risk than you are comfortable with.

A financial planner can help you create a strategy, placing your goals and objectives at the centre. Saving on tax is a by-product of good planning.

Please don't hesitate to contact a member of the team to find out more about your investment options.

Please note:

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