Market View
Tax year end planning 2025

Date 21 February 2025

Author Ola Adeosun

Reading time 6 minutes

At a glance

- As tax year end is just a few weeks away, we summarise the incoming tax rule changes.
- Namely, the removal of domicile as the key determinant for UK Inheritance Tax exposure on foreign held assets.
- It is essential for individuals to be well-informed of their tax allowances ahead of the 5 April deadline.

In the October 2024 Budget, Chancellor Rachel Reeves announced significant tax increases aimed at generating £40 billion in additional tax revenue.

One of the most notable changes is the removal of domicile as the key determinant for UK Inheritance Tax (IHT) exposure on foreign held assets. Additionally, from April 2027, unused pension funds will become part of the estate for IHT purposes, affecting individuals who had planned to defer pension withdrawals for future generations.

Maximising pension contributions

Pensions legislation continues to remain a political football. The removal of the lifetime allowance cap was a welcome change in April 2024, but the October 2024 Budget introduced another major change—pension funds will be subject to IHT from April 2027. This means that for individuals aged 75 and above, there is a risk of double taxation on death, as the pension fund will be subject to both IHT and income tax when withdrawn by beneficiaries.

Despite these changes, pensions remain one of the most tax-efficient ways to save for retirement, given the tax relief available. The annual allowance for the 2024/25 tax year is £60,000 gross for those with earnings below the threshold income of £200,000.

For those with threshold income above £200,000 and adjusted income exceeding £260,000, the annual allowance could be tapered to as little as £10,000. The ability to carry forward unused allowances from the previous three tax years remains, potentially allowing contributions of up to £200,000 gross (£160,000 net) depending on individual circumstances.

Individuals can contribute the lower of their annual allowance or relevant earned income in a particular tax year, while those without earnings can contribute up to £2,880 net (£3,600 gross, inclusive of basic rate tax relief).

UK resident non-domiciled individuals

From 6 April 2025, domicile will no longer determine IHT liability on non-UK situs assets. Instead, individuals will become subject to UK IHT once they have been UK tax residents for 10 out of the last 20 years.

New arrivals to the UK, who have not been UK residents at any point in the last 10 years, will benefit from the foreign income and gains regime, allowing them to remit some types of overseas income and gains to the UK tax_free in their first four tax years of residency.

For existing UK resident non-domiciled individuals who previously paid tax on a remittance basis, a temporary repatriation facility may be available. This would enable them to remit untaxed overseas income and gains to the UK at a tax rate of 12% in the 2025/26 and 2026/27 tax years, increasing to 15% in the 2027/28 tax year.

UK resident non-domiciled individuals and those with overseas trust structures with UK resident settlors or beneficiaries should urgently review their arrangements ahead of the introduction of the new regime on 6 April 2025.

Tax-efficient savings and investments

Individual Savings Accounts (ISAs) provide tax-free growth and income, allowing individuals to invest up to £20,000 per year without incurring income tax or capital gains tax (CGT). Parents or guardians can contribute up to £9,000 annually into a Junior ISA for children under 18.

On death, a surviving spouse can inherit the ISA allowance of the deceased, ensuring the continuation of tax benefits.

Enterprise Investment Schemes (EIS) and Venture Capital Trusts (VCTs)

Investing in EIS and VCTs can help individuals with significant tax liabilities reduce their overall tax burden.

EIS Investments qualify for 30% income tax relief on contributions of up to £2 million (provided at least £1 million is allocated to knowledge-intensive companies). Gains from EIS investments are CGT-free after three years, and income tax relief can be carried back to offset tax from the previous year. EIS can also be used to defer CGT liabilities if the investment is made within one year before or three years after a gain is realised.

VCT Investments also offer 30% income tax relief, up to a £200,000 annual limit. Additionally, dividends from VCTs are tax-free, and there is no CGT on disposal.

Income tax bands (2024/25)

- Personal Allowance: £12,570 (phased out above £100,000).
- Basic Rate (20%): Up to £37,700.
- Higher Rate (40%): £50,270 - £125,140.

- Additional Rate (45%): Above £125,140.

Be aware of the 60% Tax Trap:

Individuals earning between £100,001 and £125,140 face an effective tax rate of 66% (including National Insurance) if employed, or 62% if self-employed, due to the gradual removal of the personal allowance. Strategies to mitigate this include:

- Making pension contributions
- Charitable donations
- Using salary sacrifice (if supported by an employer)

Capital Gains Tax (CGT)

The CGT annual exemption is now £3,000 per individual, significantly reduced in recent years.

- CGT Rates (2024/25):
  - Basic Rate: 14% for disposals on or after30 October 2024 (previously 10%).
  - Higher Rate: 24% for disposals on or after30 October 2024 (previously 20%).
  - Residential Property: 24% rate applies and the CGT must be reported within 60 days of disposal of the asset.

Transfers of assets between spouses/civil partners occur on a no gain, no loss basis, making tax planning essential. Investment losses from prior tax years can be carried forward to offset future capital gains.

Tax relief for entrepreneurs and investors

- Business Asset Disposal Relief (BADR) allows CGT at 10% for disposals up to 5 April 2025, increasing to 14% in 2025/26, and 18% from April 2026.
- Investors' Relief enables CGT at 10% on the sale of unquoted trading company shares (subject to conditions). However, the lifetime allowance has been reduced to £1 million.
- Loss Relief allows losses on unquoted shares to offset income tax (up to the greater of £50,000 or 25% of adjusted total income per year). This also applies to EIS and SEIS investments.

Inheritance tax (IHT)

- Nil Rate Band: £325,000 (frozen until April 2028).
- Residence Nil Rate Band (RNRB): £175,000 (available when a main residence is left to direct descendants). Married couples may benefit from a combined £1 million IHT exemption.
- Tapering of RNRB: Applies to estates exceeding £2 million.
- IHT Gifting Exemption: £3,000 per year, with the option to carry forward the previous year's allowance for a maximum £6,000 gift.
- Surplus Income Gifting: Gifts from excess income (if a regular pattern is established and without affecting living standards) are immediately exempt from IHT.

Taking into account the proposed increases to taxes over the coming years, it is essential that individuals maximise their available tax efficient allowances where possible as we approach tax year end.

Investors should be aware that past performance is not an indication of future performance, the value of investments and the income derived from them may fluctuate and you may not receive back the amount you originally invested.