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For further information or advice on any topics in this issue, don't hesitate to contact your local office.

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Structured Deposits

With the base rate maintained in September at a historic low, the chances are that you have a number of clients, personal or corporate, who have significant cash reserves earning a minimal amount of interest.

Due to the uncertain economic climate, clients can still be wary of investing elsewhere in which case a structured deposit account may be the ideal solution for them. These versatile and secure savings plans are simply fixed term bank deposit accounts with the interest earned linked to the performance of a stock market index such as the FTSE 100 or even a number of stocks. So clients have access to the potential growth offered by stock markets without the risks as the capital is always guaranteed at the end of the term subject to the financial security of the bank.

This can be a particularly effective solution for companies as any interest due will only be paid at the end of the term offering tax deferral opportunities. For larger sums, it is possible to build a bespoke account with a term to suit any such tax planning. If cash flow is a concern then the accounts can often be used as collateral for borrowing. By using a bespoke account it is also possible to link to just about any index imaginable which may be of interest if a company is regularly doing business overseas.

Other big markets for structured deposits are self invested pensions and offshore investment bonds where the interest earned is free of tax.

AXA Family Suntrust

This is an innovative new pension product designed to offer the benefits of a Small Self Administered Scheme (SSAS) to groups of people that have previously been excluded from being members of a SSAS such as family members or businesses that operate as a partnership.

It is an individual trust based Self Invested Personal Pension (SIPP) where all members invest together, deciding on a common approach with access to a wide range of investment options. This can offer economies of scale or access to investments outside reach of individual members. It can also be used to create liquidity for existing

SIPP clients where commercial property is the largest investment by allowing other members to join the scheme.

Other advantages are increased options at retirement with the option to take a scheme pension, which may offer higher income or greater death benefits than the alternatives such as annuity, income withdrawal or, post age 75, alternatively secured pension.

In addition, as it is not an employer sponsored contract, there are no onerous trustee duties and no requirement for employer contributions.

Taxing Times for Trusts

There has been a lot of discussion about the increase to the highest rate of income tax for high earners from next year. But imagine the outcry if the 50% rate had been brought in for any income over £1,000. This is exactly what has happened for discretionary trusts with trustees seeing at least a 25% increase in income tax with effect from 6 April 2010. Any trust income above the £1,000 mark will be taxed at 50% or 42.5% for dividends.

Given the Trustee Act 2000 duty that trustees must maximise returns without any undue risk, now would seem an ideal time for trustees to take action and review trust investments to reduce any increased tax liability from next year.

The good news is that there are ways that this tax charge can be mitigated. For example, the use of an offshore investment bond provides tax deferral as it is deemed a non income producing asset. Although on encashment any gains will be taxable at the higher rate, this could be avoided by the assignment of policy segments to non or basic rate taxpaying beneficiaries before encashment occurs.

An offshore bond provides other additional benefits:

- Beneficiaries are still able to access a regular 'income' from the bond by way of the 5% annual withdrawal of the original capital investment.

- There is no Capital Gains Tax payable when the underlying investments are altered meaning that funds can be switched without tax liability, allowing trustees to meet the Trustee Act 2000 requirements to review the trust investments regularly.

If income is not required, perhaps the portfolio could be restructured in capital growth orientated assets to make use of the trustees' annual Capital Gains Tax exemption with only 18% tax being paid on any excess.

Your local Oval consultant will be happy to discuss these solutions with you or your clients.

Investment Bonds vs. Collective Investments

Due to the considerable interest shown in the article 'Tax efficient investments' in our last issue, we now provide further details.

Historically, there have been many sound reasons for recommending investment bonds to clients such as the tax deferred withdrawal facility, fund switching without tax consequences and access to popular packaged investments such as With Profits.

However, times change and circumstances alter. Onshore investment bonds are now, in many cases, less appropriate and there are two main drivers to this.

1. Taxation changes

Until April 2008, Capital Gains Tax (CGT) was liable at the highest rate of personal income tax. Now it is fixed at a flat rate of 18%. This is, of course, after utilising the annual CGT exemption, £10,100 pa per person in this tax year.

Using an assumption of 4% pa of pure capital growth, an individual could reasonably hold up to £250,000 in investments subject to CGT, without incurring any CGT liability. Returns will vary over time, with years of higher gains seeing less of the portfolio realised; conversely for times of poor returns. Even if capital growth remains above the target 4% pa consistently then this is a good problem to have and even being forced to realise excess gains will still only currently incur 18% tax.

Contrast this with an onshore investment bond, where the growth is tax paid (rather than tax free as is often incorrectly stated). Insurance companies pay corporation tax on fund profits and must allow for an element of capital growth. Expenses can be offset in the tax calculation. When insurance funds were rapidly growing, the tax provision for capital growth could be considerably reduced by the healthy

inflow of new money. In the current environment, cash inflows are very modest so the effective rate of tax is higher and probably not much less than the basic rate of income tax.

This means any onshore investment bond holder is paying tax, indirectly without any scope for this being reclaimed. The comparison is of up to £500,000 for a couple held in CGT liable investments on which the capital growth can be effectively tax free (excess only being taxed at 18%) compared to any money in an onshore investment bond which incur non recoverable tax approaching basic rate. So, from a tax perspective, onshore investment bonds are rather less attractive.

Of course, the "top-slicing" rules may ameliorate the final income tax burden on disposal but, don't forget that for clients who are already higher rate taxpayers, top-slicing is not relevant and the entire gain will be taxed at the top rate of 40% and possibly up to 50% from April 2010 (less the 20% basic rate credit suffered internally in the bond). This renders an onshore investment bond even less attractive.



2. Technology

Until the advent of technology in recent years, it was often impractical to use the CGT allowance. Even rebasing a modest portfolio of 20 funds would result in numerous contract notes and charges with the 30 day bed and breakfast rule adding a further complication. Apart from very large portfolios, the cost and administrative hassle was simply not worth the effort for the tax saved. As a result, portfolios became ever more pregnant with a CGT liability, creating problems for longer term financial planning.

This is now largely a thing of the past, particularly through facilities such as discretionary fund management and improvements in technology. It is now possible to easily lock in all or some of a portfolio gain up to the available CGT allowance at no cost and perform investment transfers such as 'Bed and ISA'.

So in conclusion as part of good financial planning, clients' existing arrangements should be reviewed. In many cases, a move from onshore investment bonds to a portfolio of CGT liable investments will be to the client's advantage in terms of tax liability, active management, simplified ongoing administration, and improved flexibility.