Guide to ISAs

What is an ISA?

ISA stands for Individual Savings Account. These were introduced on the 6th April 1999. At that time the Government promised that ISAs would available for at least 10 years. ISAs are designed to encourage savings and allow you to invest from as little as £10 up to a Maximum of £7,000 each tax year.

ISA's are tax efficient accounts. This is to say that any ISA which are interest bearing are tax free. Equity based ISA's that produce dividends are liable to a 10% tax credit. This means that although some ISA's are no longer tax free they are still taxed more favourably than other savings and investments.

This is different to many other investments, such as ordinary bank or building society accounts. Normally tax is deducted taken from any interest before it is added to deposit accounts.

(Please note: there are special rules for people that do not pay Income Tax and choose to save or invest in Bank / Building Society accounts. We will be able to explain these rules).

Who can have an ISA plan?

There are certain rules regarding as to who can have an ISA plan. Since ISAs were first introduced there have been restrictions as to who can subscribe to a plan.

In order to make a contribution to an ISA plan you must be UK tax resident (or perhaps a Crown Employee that are serving overseas).

In addition to this there are age limits:

Anyone aged 16 or over may invest up to £3,000 into a cash ISA. The plan may be a Cash Mini ISA or the cash component of a Maxi ISA.

People over the age of 18 may elect to invest their money in a Stocks & shares ISA.

If you have any queries about your eligibility for an ISA, please contact us now.

What are the different types of ISA?

- ISAs come in two different versions so that they can cater for the different needs of investors. It is possible to have a mixture of the different types but before you do this you should refer to our section on 'What are Maxi and Mini ISAs?'
- Stock and Shares ISA - These allow you to invest in either Company Shares quoted on a recognised Stock Exchange, investment trusts, unit trusts or OEICs. You can, if you wish, mix and match the investments.
- Cash ISA - These allow you to invest in a deposit account with a bank or building society.

Why would I want an ISA?

ISA’s are an excellent way for taxpayers to save. Cash ISA’s and some other interest bearing ISA’s are tax fee where as dividend bearing ISA’s are classed as tax efficient, only being liable to a 10% tax credit. This means that for most people they are still paying less tax then through other types of saving plans.

How much can I invest in an ISA?

Under current rules you can invest during any single tax year up to a total of £7,000 into a single Stocks and Shares Maxi ISA . (a tax year runs from 6th April to the following 5th April).

Although the total contribution limit is £7,000, there are individual limits on how much can be invested into the various components of an ISA.

- Stocks and Shares ISA - It is possible to invest up to the £7,000 Maximum into one of these. However this is only possible if you have not paid money into any other ISA plan in the same tax year.
- Where money has been paid into another type of ISA during the same tax year then the limit is reduced to £4,000.
- Cash ISA - Amounts up to a Maximum of £3,000 can be paid into a Cash ISA in any single tax year.

What are Maxi and Mini ISAs?

During each tax year you may invest in one ISA or you may decide to spread your money across MINI ISAs. Whether or not you have more than one version of an ISA; the annual investment limit remains the same at £7,000 for the current tax year.

Maxi ISA

- Any provider that wishes to offer a Maxi ISA must include the opportunity for you to invest in stocks and shares (including unit trusts, Oeics and investment trusts).
- You are allowed to invest your total annual ISA allowance in a Stocks & Shares Maxi ISA.
- The ISA provider can elect to offer a Cash component alongside the Stocks & Shares component if they wish.

The overall investment limit into a Maxi ISA equals £7,000 for each of the tax years until 5th April 2006.

Mini ISA

- Each Mini ISA may only contain a single component of the allowable investments.
- If you wish to spread your investment amongst two different types of ISA plan then you must establish Mini ISAs. Each of the plans could be with a different provider.
- If you do not make contributions to the Maximum limit under each of these investment components, the balance cannot be carried forward to another tax year or transferred to a different ISA component.
- You must be careful not to invest money in a Mini ISA if there is any likelihood you will later in the same tax year wish to invest your full ISA contribution allowance into a Stocks and Shares ISA.

Summary of the Maximum amounts you may pay to an ISA plan

Component	Mini ISA (Contributions may be made to each different component during the same tax year)	Maxi ISA (Contributions may only be made to one of different components during the tax year)
Cash	Up to £3,000	Up to £3,000
Stocks and shares	Up to £4,000	£7,000
Overall Limit	£7,000	£7,000

How many ISAs can I have?

Although over time you may end up with many ISA plans, you may only contribute, during any single tax year, to one Maxi ISA or up to two Mini ISAs - one for each type of ISA component.

Each tax year you may decide to contribute to an ISA product (either Maxi or Mini) from a different ISA provider to those you have contributed to before.

What are the tax benefits of an ISA?

Under current legislation ISAs have considerable tax incentives over other forms of investments or savings.

- Cash ISAs are free of income tax. Other types of ISA are not necessarily free of income tax -it depends what they are invested in. Since 6 April 2004, any income from shares or share-based unit trusts within an ISA is paid with tax at 10% already deducted and this cannot be reclaimed. But there is no tax on any other type of income - for example, interest from gilts or corporate bonds - held within the ISA.
- You pay no tax on any capital gains achieved by your ISA investments (please note any losses cannot be offset against gains that are subject to Capital Gains Tax).
- ISA's are not necessarily free of income tax -it depends what they are invested in. Since 6 April 2004, any income from shares or share-based unit trusts within an ISA is paid with tax at 10% already deducted and this cannot be reclaimed. But there is no tax on any other type of income - for example, interest from gilts or corporate bonds - held within the ISA.
- ISA’s are free of capital gains tax. So, if your ISA increases in value, you make a 'capital gain', but you do not have to pay capital gains tax on this increase.

- You may withdraw your money at any time without losing any of the tax advantages.
- There is no requirement for you to declare income and/or capital gains from your ISA plans to the Inland Revenue. You don't even need to mention that you have an ISA on your Tax Return.

How long must I keep my ISA plan?

One of the major attractions of ISA plans is that they offer you excellent access to your money. You may withdraw your money at any time without losing any of the tax relief granted to your plan.

However most incur an initial cost when setting up so if you encash early this may mean you get less back than you originally invested.

Some ISA plans may run for a fixed period or require you to give notice of withdrawal. With these particular plans you could lose some interest or bonuses should you elect to withdraw your money early. You should always read the terms of your ISA plan carefully and pay particular attention to any conditions applying to withdraw of your money.

Please note that if you invest in a Stock& shares ISA you may not get back all the money you put in. This is more likely if you withdraw you money during the early years of your investment

What are stakeholder ISAs?

From 6 April 2005, new stakeholder products became available. To earn the name ‘stakeholder’ the products have to meet conditions designed to ensure that the products are straightforward and good value.

There are five stakeholder products:

- stakeholder deposit;
- stakeholder medium-term investment product (MTIP), which is a type of unit trust or similar investment;
- smoothed MTIP, which is similar to with-profits life insurance;
- stakeholder pension; and
- child trust fund stakeholder account.

The first three: the stakeholder deposit, MTIP and smoothed MTIP are available in both ISA and non-ISA versions.

Stakeholder ISAs replaced CAT-standard ISAs from 6 April 2005 onwards. However, if you took out a CAT-standard ISA before that date, it will continue to meet the CAT standards. (‘CAT’ stands for fair Charges, easy Access and decent Terms.)

Neither the stakeholder conditions nor the CAT standards guarantee the performance of a product. They do not mean that the government recommends that product or that the product is necessarily suitable for you. But they do provide a useful benchmark against which to compare other products.

What are the Stakeholder conditions?

Cash ISAs - Stakeholder deposit account

- There are no charges to pay on stakeholder cash ISAs.
- The minimum deposit cannot be higher than £10.
- You can pay into the account in any of the following ways: cash, cheque, direct debit, standing order, direct credit (also called BACS or automated transfer).
- You can make unlimited withdrawals.
- Withdrawals should be paid to you within seven days or less.
- The interest rate paid must be no less than 1 per cent below the Bank of England base rate.
- If the Bank of England rate goes up, the minimum interest rate must also go up within one month.

Stocks and shares ISAs - Stakeholder medium-term investment products (MTIP)

- Annual charge limited to 1.5% of the fund during the first ten years and 1% thereafter.
- The minimum deposit cannot be higher than £20.
- No more than 60 per cent of the fund is invested in riskier assets such as shares.
- You can pay into the account in any of the following ways: cheque, direct debit, standing order, direct credit (also called BACS or automated transfer).
- The prices at which units or shares in the fund are bought and sold must be the same and the price should be published daily.

Extra terms apply to the smoothed MTIP:

- Some of the return in good years is paid into a 'smoothing account' to be used to top up the return in bad years.
- If the smoothing account needs extra capital, policyholders can be charged extra.
- Managers must make available information about their policies on smoothing and charging.
- The whole with-profits fund and the whole smoothing account, apart from specific deductions allowed by law, are for the benefit of policyholders.

What happens if I die?

Any ISA plans you hold will end on the date of your death. No tax will become due on any income or capital gains that have been achieved up to that date. However, if the plan continues after your death, then your personal representatives will be liable for taxation on any subsequent income or capital gains.

The value of any ISA plans will be added to the rest of your assets when calculating the value of your estate for Inheritance Tax purposes.

Under the terms of a life insurance ISA the proceeds of the policy will be payable at the time of your death. Although there would not tax to pay on the policy proceeds built up during you life, however if any interest is added by the life insurance company because of late payment of the claim, then this interest would be subject to taxation.

Is an ISA right for me?

In a similar way to any savings or investment scheme, before making any financial commitments like an ISA, you should give careful consideration as to whether this is the correct course of action for you.

Ensure you are satisfied the money could not be put to better use. If you have a large outstanding credit card balance, or other debts, you may wish to consider repaying this debt before you put money aside into any savings or investment scheme. We will be able to assist you in this matter. Please contact us with any questions.

If you decide to save or invest for the future, then careful thought must be given to the time period that you can afford to leave your money tied up. The use a Stock & shares ISA is normally suitable for people looking to save for the medium to long term (i.e. five years or more). A Mini Cash ISA (or the cash component of a Maxi ISA) might prove to be a suitable home for short-term savings. But once you have saved up to the limit of £3000 in one tax year, you can not put back any cash you withdraw. It's the money you actually put in that counts towards the annual £3000 limit.

Those people that decide to invest in a Stocks & Shares ISA must also take into account their personal attitude to investment risk. Please remember the value of your investment in these types of ISA can go down as well as up. We will be able to assist you when considering such matters.

Can I change the savings or investments in my ISA plan?

You have the right to transfer an ISA run by one manager to an ISA of the same type run by another manager. But ISA managers do not have to accept a transfer. Watch out for transfer charges.

You cannot transfer from an ISA of one type (for example cash) to a different type of ISA (for example stocks and shares).

Should you wish to include new investment or savings opportunities that are not provided from your current ISA manager then you may have to transfer you money to another manager.

I have an existing PEP or TESSA investment plan?

Since April 1999 both Personal Equity Plans (PEPs) and Tax Exempt Special Savings Accounts (TESSAs) have been replaced, in respect to the starting of any new plans, by ISAs.

If you hold an existing PEP investment plan you may maintain it or even transfer all or part of it to a new PEP Manager. This facility allows you to change the underlying investments or perhaps move your money to a plan that has lower charges.

Tax-exempt special savings accounts (TESSAs) are no longer available, and the last TESSAs matured on 5 April 2004. You had six months from the date your TESSA matured (in other words up to 5 October 2004 in the case of the very last TESSAs) within which to transfer to a tax-free ISA.

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