

Is There Life in Investment Bonds?

Recent Budget changes to Capital Gains Tax have a major impact on Investment Bonds. Chris Budd of Ovation Finance Limited investigates.

In his recent budget, Alistair Darling confirmed significant changes to capital gains tax, coming into effect on 6th April, 2008. This has a major impact on the type of vehicle in which you hold your investments, notably to the detriment of the Investment Bond.

In brief, he has set a flat rate of 18% on all capital gains. Indexation allowance and taper relief have gone. The tax on investment growth, therefore, is simply calculated by taking the current value, minus the purchase value, and taxed 18% on the difference.

Investment Bonds have been one of the major types of investment recommended by advisors over the years. There are several reasons for this, but one of them has been the ability to withdraw 5% of the amount invested, for 20 years, from the Bond as income without paying any tax.

Deferment

In fact, not all Bond holders are aware that their Investment Bond actually pays basic rate tax within the fund. For a basic rate tax payer, this 5% withdrawal facility is therefore largely irrelevant, as they wouldn't be paying any higher rate tax anyway. For a higher rate tax payer, this does allow deferment of any extra tax, although the 5% facility is only really paying back the capital that you invested in the first place.

Following these changes, the vast majority of Investment Bond holders could be better off considering a Unit Trust instead. In this way, they would only be paying 18% tax on any growth, with an annual allowance of up to £9,600 growth tax free. The net rate is therefore likely to be much lower than under the Investment Bond.

IHT Planning

There are still circumstances where Investment Bonds are favourable, particularly for the higher rate tax payer. There are certain planning

opportunities, and inheritance tax planning can still use certain features of Investment Bonds.

For many people, however, structuring their income rather differently may be to their advantage. For example, why not consider retaining sufficient amount on deposit to pay the next, say, five years income, with the remainder being invested. In five years time, sufficient capital can then be encashed to pay for the next five years income. In this way, tax is paid at capital gains tax rates, not income tax rates.

Of course, any such planning must be only done carefully and preferably in conjunction with your financial advisor. You should also not rush to cash your Investment Bond, but only do so once you have reviewed your investment with a financial advisor, who can take into account all of your circumstances.

This article is for general information only. Remember past performance is not a guide to future performance and investments can go up as well as down. If you have any doubts in respect of your own personal circumstances you should request a full review with an independent financial adviser to get their help.

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email: enquiries@ovationfinance.co.uk www.ovationfinance.co.uk

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