



DENTAL & MEDICAL
FINANCIAL SERVICES



KEY GUIDE

Making the most of ISAs

Introduction

AN INTRODUCTION TO ISAs

Individual Savings Accounts, universally known as ISAs, began life as relatively simple savings plans in 1999, but over the past 25 years the rules surrounding them have become ever more complex. While there have been calls to make the regime simpler and more accessible, until the Autumn Statement 2023 in recent years the government had shown little interest in ISAs. For example, the main contribution limit has been unchanged since April 2017. The Autumn Statement simplified some of the administrative complexities but also removed one investment opportunity from 6 April 2024.

The government's website says there are only four categories of ISA – cash ISAs, stocks and shares ISAs, innovative finance ISAs, and Lifetime ISAs – but variants exist for specific investment needs.

This guide will explain how the main variants work, in order of their original launch date.

Please note that all examples included in this guide are fictitious.

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The main categories of ISA

Despite the different choices available, all ISAs have a number of features in common. For example, they all enjoy tax privileges, a consequence of which is that the amounts that you can invest in each type, and in all ISAs, are generally subject to annual limits. ISAs may only be run by HM Revenue & Customs (HMRC) approved ISA managers.

Planning point

Make the most of ISAs – they are all free of UK income tax and capital gains tax.

The ISA family can be divided up in several ways – hence the differing headcount. One way of looking at it is to consider them in terms of when they first became available:

- **Basic ISA** The original ISA lives on as a plan with two investment components: stocks and shares or cash. The two are interchangeable, so you can transfer from a stocks and shares ISA to a cash ISA, or vice versa.
- **Junior ISA (JISA)** The JISA is available to children under 18 who do not already have a Child Trust Fund (CTF) account. Again, both cash and stocks and shares variants are available.
- **Lifetime ISAs (LISA):** The LISA, launched in April 2017, is aimed at encouraging saving for first home purchase or retirement by adults under the age of 40. It provides investors with a government bonus, but comes with penalties if funds are withdrawn before age 60, other than for a first home purchase. The choice of LISA providers is much smaller than for the Basic ISA.

You will incur a LISA government withdrawal charge (currently 25%) if you transfer the funds to a different ISA or withdraw the funds before age 60 (other than for purchasing your first home) and you may therefore get back less than you paid into a lifetime ISA.

By saving in a LISA instead of enrolling in, or contributing to an auto-enrolment pension scheme, occupational pension scheme, or personal pension scheme:

(i) you may lose the benefit of contributions from your employer (if any) to that scheme; and (ii) your current and future entitlement to means tested benefits (if any) may be affected.

- **Help to Buy ISA** This type of ISA is no longer available to new investors. In practice, it was a variant of a cash component basic ISA, aimed at first home buyers. The plan has been replaced by the Lifetime ISA (see above), but existing investors can continue making contributions until November 2029.

ISA ELIGIBILITY

ISA investors must be resident in the UK, or a non-resident Crown employee working overseas and subject to UK tax on their earnings. Spouses and civil partners of eligible non-resident Crown employees can also contribute if they are themselves non-resident.

An ISA can only be arranged on an individual basis (so cannot be held jointly) and it cannot be held in a trust. However, ISAs can effectively be inherited by a surviving spouse or civil partner (see 'Inheritance' below).

Age eligibility for starting an ISA depends upon the type of plan, as shown in the table below.

Type of ISA	Opening age range	Notes
Basic ISA	18 upwards generally	In 2023/24 16- and 17-year-olds may start a basic ISA but can only choose the cash component. This option will not be available in 2024/25.
Junior ISA	Under age 18	Investors cannot also have a Child Trust Fund (CTF). Broadly speaking, this means JISAs are available to any child who was born after 2 January 2011, or who was born during the CTF government provision, but whose CTF monies have been transferred into a JISA.
Lifetime ISA	18-39	Contributions cannot be made from age 50 onwards.
Help to Buy ISA started before 1/12/19	16 upwards	No new plans can be started, but existing investors can continue to contribute. Help to Buy bonus must be claimed by 30 November 2030.

Planning point

There is nothing to report about ISAs on your tax return.

ISA INVESTMENT AND ACCOUNT STRUCTURES

ISAs, JISAs and LISAs currently have two possible investment components:

1. The stocks and shares component

Shares listed on any recognised stock exchange and certain other exchanges, such as AIM (alternative investment market), can be held in the stocks and shares component of an ISA. Some, but not all, AIM shares are eligible for inheritance tax (IHT) business relief after two years of ownership.

- All Financial Conduct Authority (FCA) authorised retail funds – i.e. virtually any trust, open-ended investment company (OEIC) or undertaking for collective investment in transferable securities (UCITS), including exchange traded funds (ETFs) – are eligible for ISA investment.
- Corporate bonds and EEA government securities are also eligible investments, regardless of the term to maturity.
- Cash can be held in the stocks and shares component without restriction.
- The stocks and shares component can also include life assurance, although this is now extremely rare.

Investing in shares should be regarded as a long-term investment and should fit in with your overall attitude to risk and financial circumstances. The value of investments can fall as well as rise. You may get back less than you invested.

2. The cash component

This may be invested in bank or building society deposits as well as money market unit trusts that hold deposits rather than securities. National Savings & Investments offers two variable rate cash ISA products, the Direct ISA and the Junior ISA. At the time of writing there were only handful of providers that offered a cash component LISA.



Innovative Finance ISA

The Innovative Finance ISA was launched in April 2016, although regulatory approval and supply/demand issues meant a slow start from which it never recovered. These ISAs permit investment in cash and two specialist financial products:

- Peer-to-peer (P2P) loans – loans arranged to other people or businesses without an intermediary bank being involved.
- Crowdfunding debentures – investing in a business by buying its debt.

In both instances, the businesses involved are usually unlisted and small. Whereas the Financial Services Compensation Scheme protects up to £85,000 of deposits held in the cash component of basic ISAs, there is no such protection for peer-to-peer loans or crowdfunding debentures. A restriction limiting investment to sophisticated or high-net-worth individuals generally applies to crowdfunding.

Financial Conduct Authority (FCA) reforms to the innovative finance sector have prompted the P2P market to contract significantly, with the largest participants no longer offering retail products.

From 2024/25 Innovative Finance ISAs will also be able to invest in Long Term Asset Funds and open-ended property funds with extended notice periods.

ISA ACCOUNT INVESTMENT LIMITS

For 2023/24 the rule is that in any one tax year, you may only subscribe to one of each type of ISA. This means that in 2023/24, subject to eligibility, you can subscribe to:

1. a basic ISA with a stocks and shares component;
2. a basic ISA with a cash component or, if started before 1 December 2019, a Help to Buy ISA (a small number of providers incorporate both types within the one ISA wrapper);
3. an Innovative Finance ISA.
4. a LISA.

If an ISA is transferred in full, the current one-ISA-per-type-per-year rule applies in 2023/24. Any subscription made at any time in the tax year during which the transfer is made is treated as a subscription to the recipient ISA.

From 2024/25 the one plan, per type, per tax year rule will be dropped, allowing, for example, investment in three stocks and shares ISAs over the tax year from three different providers. It will also become possible to partially transfer a current year ISA.

Planning point

The total contributions limit across all ISAs for adults is £20,000 per tax year for 2023/24.

EXAMPLE

Using ISA limits 2023/24

Lindsay is 37 and on 19 April 2023 started a LISA with a subscription of £4,000. If she wants to maximise her ISA investment in 2023/24 to use the full £20,000 limit, her options include:

Type of ISA	Option 1 Amount £	Option 2 Amount £	Option 3 Amount £	Option 4 Amount £
Basic – cash	16,000	Nil	5,000	10,000
Basic – stocks and shares	Nil	16,000	11,000	6,000
Total	16,000	16,000	16,000	16,000

In 2023/24 Lindsay could only arrange one of each type of ISA, but if she has existing ISAs in any category, she could use the full transfer route to make contributions to a new ISA.

The maximum overall investment across all ISAs in 2023/24 (and 2024/25) is £20,000. However, there are sub-limits for LISAs, JISAs and existing Help to Buy ISAs:



- For **LISAs** the maximum subscription is £4,000 per tax year.
- For **JISAs**, the maximum contribution is £9,000. In addition, for 2023/24 only, a 16- or 17-year-old can open and subscribe £20,000 to a cash component basic ISA.
- The maximum **Help to Buy** subscription for an existing plan is £200 a month.

Transfers

The ISA transfer rules are complex (albeit simplifying in 2024/25) and leave discretion for providers on whether to accept transfers in, although they are obliged to allow full transfers out. Funds transferred between ISAs or between the cash and stocks and shares components generally do not count as fresh subscriptions, but can complicate the calculation of subscription limits.

Transfers may involve costs and/or penalties and may result in lost bonuses. Any transfer should only be undertaken after seeking expert advice.

Flexibility

Some, but not all, ISA providers take full advantage of the legislation and allow you to withdraw and replace cash sums during the same tax year without the replacement counting as a fresh subscription. This flexibility is not available for LISAs or JISAs and is severely restricted in the case of Help to Buy ISAs.

EXAMPLE Using ISA flexibility

Graeme had a cash ISA worth £60,000, having invested the maximum £20,000 subscription in early May 2023. Seven months later he was in the process of moving home and needed £40,000 cash to complete his purchase. He had this amount in a fixed term deposit which was due to mature in March 2024, but he did not want to pay an interest penalty to gain early access. Instead he used the flexibility his ISA offers to withdraw the sum he needed in December 2023 and then replenished his ISA with the monies from his maturing deposit before 6 April 2024.

Planning point

ISAs are effectively inheritable by a surviving husband/wife or civil partner.

Inheritance

ISA rules allow the value of any ISA to be inherited and used as an “additional permitted subscription” (APS) by a surviving spouse or civil partner. Generally speaking, the ISA tax benefits remain during the administration period and all investments plus any subsequent growth or return form part of the APS.



The ISA's tax advantages are thus able to outlive the original ISA owner, with their ISA holdings and tax benefits normally being transferable in full to the survivor. This can have important estate planning benefits, effectively turning what is an individual investment into a joint investment. In some circumstances the inheritability of ISAs will mean that pension arrangements can be left untouched, which may prove useful for inheritance tax planning.

TAX TREATMENT OF ISA INVESTMENTS

All ISAs enjoy the same tax treatment on invested funds.

Stocks and shares component

All capital gains and dividends are free of UK tax. Foreign withholding taxes may apply, however. Dividends received within an ISA are ignored when considering your available dividend allowance (£1,000 in 2023/24 and £500 in 2024/25). Outside of an ISA the tax on dividends exceeding the dividend allowance ranges from 8.75% for basic rate taxpayers to 39.35% for additional rate taxpayers.

Interest received on bond and cash investments is tax free and does not count towards your personal savings allowance.

If AIM and similar shares are held in an ISA, the normal inheritance tax business relief rules apply. Broadly speaking, these mean that many AIM shares are IHT-free after they have been held for two years.

Cash component ISA investments

All interest is tax free.

LISA

Additional tax benefits apply to LISAs and Help to Buy ISAs (started before 1 December 2019). LISAs offer eligible investors a 25% tax free government bonus on their subscriptions until they reach age 50. So, for example, if you subscribe the maximum of £4,000 in a tax year, the government will add an extra £1,000 to your LISA.

This generosity comes with strings attached. If you withdraw funds from a LISA before you reach age 60, a penalty will apply to the amount withdrawn unless:

- your LISA is at least 12 months old and you are using the funds towards a first-time purchase of a home valued at up to £450,000 (anywhere in the UK); or
- you have become terminally ill.

The standard penalty rate is 25%, a figure that applies to both the government bonus and encashment penalty. As the example below shows, the 25% exit charge is not just the clawback of the 25% bonus, but includes also any returns on the bonus and an additional 6.25% charge on the contribution made by the saver.

EXAMPLE The LISA penalty

Harry made a contribution of £3,000 to a LISA in September 2022, to which the 25% government bonus of £750 was added. Over the following fifteen months, the LISA grew in value to £4,000. If Harry decided to withdraw £1,000 to spend on a new computer in December 2023, he would have received only £750 after the 25% penalty had been deducted.

Help to Buy ISA – started before 1 December 2019

The extra tax benefits for the Help to Buy ISA only apply if the funds are used to finance a first-time buyer's home purchase. The maximum value of the property to be bought is £250,000 (£450,000 in London). Purchases may be made on a joint basis, meaning that a couple could each use a Help to Buy ISA to buy the same property.

For eligible first-time buyers, the government provides a tax free bonus equal to 25% of the ISA's value. The bonus is subject to a minimum of £400 (implying a minimum ISA value of £1,600) and a maximum of £3,000 (for ISAs valued at £12,000 or more). No bonus payments will be made after 30 November 2030 or on transfer to a LISA (see above).

If the Help to Buy ISA funds are not used for first-time property purchase, there is no bonus payable, but the normal cash component tax freedom for interest still applies. The Help to Buy ISA was withdrawn for new investors from 1 December 2019, but exiting investors can continue to contribute until November 2029.

Planning point

Making a choice between ISAs and your pension is not a straightforward decision and needs expert advice.

Your capital is at risk if you make peer-to-peer loans or invest in crowdfunding debentures. Any such lending is likely to be highly illiquid, meaning that you may not be able to access your monies until the loan is repaid, assuming there is no default.

The value of investments and the income they produce can fall as well as rise. You may get back less than you invested.

For ISAs investors do not pay any personal tax on income or gains, but ISAs do pay unrecoverable tax on income from stocks and shares received by the ISA managers.

Tax treatment varies according to individual circumstances and is subject to change.

Stocks and Shares ISAs invest in corporate bonds; stocks and shares and other assets that fluctuate in value.

Alternative Investment Market (AIM) Business Relief schemes (BR) invest in assets that are high risk and can be difficult to sell such as shares in unlisted companies. The value of the investment and the income from it can fall as well as rise and investors may not get back what they originally invested, even taking into account the tax benefits.



HOW WE CAN HELP

Investment is a specialist area and can only be conducted by authorised advisers. We can:

- Advise you whether ISAs make sense for you in terms of your particular needs and objectives.
- Advise which ISA variants are most suited to your circumstances.
- Review your existing ISA holdings to see if they still meet your aims and circumstances.
- Advise you on whether to bring Child Trust Fund investments under the JISA umbrella and the opportunities this offers.
- Advise you on the options to deal with a maturing or matured Child Trust Fund.
- Explain the relative advantages and disadvantages of LISAs and pensions.
- Set out the way in which ISAs can form part of your estate planning arrangements.
- Advise you on strategies to minimise the tax on your investments outside ISAs.
- Review your investments from time to time as agreed, to ensure that they continue to match your needs and circumstances.



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