**Inquiry on First Home Ownership**

I see two main (and relatively straightforward) methods of helping us first home buyers to overcome the present and ongoing housing crisis - (1) reduce property investor impact, and (2) encourage people to save towards their home. Practical options:

=> Reverse (or at least reduce) the dramatic impact of property investors. Increase the level of capital gains tax on investment properties, and overhaul and/or reduce the tax write-offs and timing, and other excessive incentives of negative gearing. Our tax system is designed to reward and encourage greed and debt (hence the record and rapidly rising levels of household and investor debt). This *must* be changed. The tax odds are well and truly stacked against first home buyers. The devastating effects of this are all too obvious.

=> Stop punishing people who save. Instead, encourage them to save as large a deposit as possible to reduce the size of their mortgage debt. Many people now renting would use current low interest rates to buy they own home *if* they could *effectively* save towards it. They are a number of ways of doing this:

-> remove punitive tax rates on non-salary income of wage and salary earners, and (really) abolish provisional tax (yes, it still exists).

-> allow mortgage payments to be tax deductible, like they are in the US, but *only to first home buyers*. There would need to be safeguards put in place to avoid exploitation and abuse of this system by those not entitled to it. The First Home Owners Grant has shown the type of abuse that can happen.

-> immediately introduce *Individual Savings Accounts (ISAs)* like those available in the UK, where the income from certain interest-bearing accounts is tax free. Design these accounts for Australia so that the money (both saved into them and the income re-invested back into them) is restricted to the purchase of a first home.

This pdf file => ISAs_UK.pdf from the UK Department of Inland Revenue provides background details and answers about these accounts.

I believe many other issues (eg, land release, high migration levels, stamp duty and other taxes) are obvious, but political factors and self-interest mean it is highly unlikely that they will be effectively dealt with.

There *are* real answers to this crisis, and most do not appear to me to be rocket science. I hope your investigation will have a real impact, and help lead us to the opportunity of home ownership.

Kind regards,
Mark Nelson

Inland Revenue

# ISAs, PEPs and TESSAs

Everyone who can afford to should try to save at least a little. The Government has designed ISAs to provide several ways for you to save - without paying tax on what you earn from your investment, and you can put money in and take it out whenever you want to.

For example, you could start with a few pounds in a simple cash ISA, for 'rainy day' savings that you need to get at quickly.

Or you might consider investing in a stocks and shares ISA, for longer-term saving.

You could also choose a life insurance ISA for longer-term saving, with some built-in cover in the case of your death.

This booklet will give you the information you need to help make your savings decisions.

This booklet also gives information on TESSAs and PEPs for savers who already have these.

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# About this booklet

The Individual Savings Account ('ISA' for short) is a tax-free scheme designed by the Government to help you save. This booklet will tell you about ISAs and how they work, so you can decide if saving in an ISA would be right for you. It is divided into four parts.

The first part gives you just the basic facts - the essentials you'll need to know in order to make an informed choice.

The second part should answer most other questions you may have.

The third part goes into specific subjects in greater detail.

The fourth part gives some information about TESSAs and PEPs for savers who have these. TESSAs and PEPs were closed to new investors from 6 April 1999.

If you have any general questions about the tax rules for ISAs, TESSAs and PEPs that this leaflet does not cover, you can call the Inland Revenue ISA Helpline on **0845 604 1701**, between 8.30am and 5.00pm Monday to Thursday and between 8.30am and 4.30pm on Friday (calls are charged at local rates).

# ISAs (Individual Savings Accounts)

# The basic facts

## So, what is an ISA?

An ISA is a type of savings account. Basically, if you save in an ISA you are entitled to keep all that you earn from that investment and not pay any tax on it. This is not the case with, for example, an ordinary bank or building society account unless you are a non-taxpayer - see our booklet IR110 'Bank and Building society interest. A guide for savers̀ Details of how to obtain this are on page 27.

ISAs began on 6 April 1999 and will be around for at least 10 years from that date. You can start with small amounts and save up to £7,000 each tax year until 2005/2006, and up to £5,000 in each tax year from 2006/2007. A tax year runs from 6 April to 5 April the following year.

## Why would I want one?

ISAs are a good way to save. The important thing about them is that you do not have to pay tax on the money you earn from them. You can put money in and take it out whenever you want, and you don't even have to tell your Tax Office that you have an ISA.

## Where can I get one?

You can get ISAs by going to an ISA manager. These include banks, building societies, National Savings, some supermarkets and retailers, friendly societies, insurance companies, unit and investment trust companies, financial advisers, fund supermarkets and stockbrokers. Your ISA manager will look after your account for you.

## Are they flexible?

Yes. The ISA scheme has been designed to provide different ways of saving to meet people's different needs. You can plan for the short term, or put your money away for much longer.

There are three ways - called 'components' - in which your money can be invested: cash savings, stocks and shares, and some specially designed life insurance policies.

- Cash ISAs may be suitable for short-term savings, so that you can get at your money easily.

- Stocks and shares ISAs may be appropriate if you can afford to leave your money untouched for longer than, say, five years, though your investment may go down in value as well as up, and you are not guaranteed to make a profit.

- Life insurance ISAs are also for long-term saving and offer some built-in life cover in the case of your death. Again, you are not guaranteed to make a profit and you may get back less than you put in, particularly if you take your money out after only a few years. However, some types of policy, including 'with profits' policies, are designed to iron out the ups and downs of the stock market.

## How do I find out about them?

ISA managers will give you details of the ISAs they offer and may provide advice about which would be right for you. (Not every ISA manager will offer every facility.) Alternatively, you could go to an independent financial adviser for help in choosing the best option. The Financial Services Authority's booklets, the *FSA guide to financial advice* and the *FSA guide to ISAs - An introduction* give more information. You can get them by calling the FSA Consumer Helpline on **0845 606 1234** (calls are charged at local rates) or from their website at www.fsa.gov.uk/consumer.

## How much can I put into ISAs?

You can put in as little as you like (subject to the ISA manager’s terms and conditions). You can put in as much as £7,000 in each of the tax years 2001/2002 to 2005/2006 and up to £5,000 in each subsequent tax year from 2006/2007.

You can pay into your ISA whenever you want. You can pay the full amount in one go, make regular payments or pay in when you like. You can stop making regular payments at any time.

## How do I get one?

Simply apply to the ISA manager of your choice. You could visit a branch, or write to them. Some companies allow you just to telephone, fax or e-mail.

What you have read so far is the basic information you need to know about ISAs.

If you want to know more, read on. The next part provides answers to further general questions about ISAs. Part three goes into more detail on specific subjects. Part four gives information about TESSAs and PEPs.

# Your Questions Answered

## Can I have an ISA?

To open an ISA you have to be aged 18 or over, or for cash ISAs aged 16 or over. You also have to be resident and ordinarily resident in the UK for tax purposes (ask your Tax Office if you are in any doubt about this).

Crown employees, such as diplomats or members of the armed forces, who are working overseas and paid by the Government are eligible to open an ISA. From 6 April 2001, the husband or wife of one of these people can also open an ISA.

You cannot hold an ISA jointly with, or on behalf of, anyone else.

## How do I choose an ISA?

**Types of ISA**

There are three types of ISA: Mini ISAs, Maxi ISAs and TESSA only ISAs. You can put money into any of the three in any tax year, but you cannot put money into both a Mini ISA and a Maxi ISA in the same tax year.

**A Maxi ISA** can include cash, stocks and shares and life insurance in a single ISA with one manager.

**Mini ISAs** mean you can have separate ISAs, with different managers, for cash, stocks and shares and life insurance.

**A TESSA only ISA** can only be opened with capital from a matured TESSA.

There are other differences between Maxi and Mini ISAs, and ISA managers can advise you about these. For more detailed information, turn to page 17.

### *Standards to look for*

The Government has laid down a set of standards to help savers find ISAs that offer reasonable **C**harges, easy **A**ccess, and fair **T**erms - which is why they're known as the 'CAT' standards.

You may want to see if the ISA you are considering meets the relevant standard. ISAs that do are likely to make this clear in their leaflets and posters.

**But remember, CAT standard ISAs will not necessarily be suitable for all savers. If a product meets the CAT standards, this does not mean that the performance of the investment is guaranteed, or that the product is approved by the Government.**

For more detailed information on the CAT standards turn to page 14.

### *What the standards promise*

Managers of CAT standard ISAs are committed to treating customers fairly. This means they will use plain English and avoid complex or misleading features. In other words, CAT standard ISAs should be simple, clear and fair.

CAT standard ISAs are available for sale on their own. Savers will not be forced to buy any other product along with a CAT standard ISA.

## How do I choose an ISA manager?

### *Things to bear in mind*

Does the ISA manager offer the kind of ISA you want? Managers may offer both Maxi, Mini and TESSA only ISAs, or only one. They may offer cash ISAs, stocks and shares ISAs and life insurance ISAs, or only one or two of these.

Some managers may offer ISAs that can include only that company's own products. Others may offer a choice of their own or other companies' products. Or they may offer 'self-select' ISAs, where you can choose from a wide range of shares and securities.

What are the charges? Make sure you know whether the ISA manager will charge for running your ISA, including any charges for withdrawals and transfers. CAT standard ISAs have limits on charges. (For more detailed information on the CAT standards, see page 14.)

All ISA managers must be approved by the Inland Revenue and authorised by the Financial Services Authority (FSA), but neither they nor any other Government Department have approved any ISAs. Approval does not guarantee an ISA manager's performance, or that the ISA investments will produce a satisfactory return.

## *Switching from one ISA manager to another*

You can transfer your ISA to another ISA manager whenever you want.

You can usually transfer simply by asking the new ISA manager to arrange the transfer. Your existing ISA manager can't stop you transferring, but they may make you pay a charge, or insist that you sell any existing ISA investments and transfer cash (this will be specified in the ISA manager's terms and conditions).

**Note**: Your ISA must be transferred directly between the two managers. You **cannot** transfer your ISA by closing it and opening a new ISA with the new ISA manager.

ISA cash, savings and investments must always remain in the same component. You cannot move funds from, say, a cash ISA with one manager to a stocks and shares ISA with another.

**You are only allowed to put money into one Maxi ISA or one Mini ISA of each type in a tax year**. So, if you want to transfer the money you have put into your ISA in the current tax year, you must transfer all of it, and any more money you want to put in this year must go into the new ISA.

You can transfer all of the money you put into your ISA in earlier years or only some of it, if you wish. However, some managers may not allow you to transfer part of your ISA (this will be in the terms and conditions). Your existing ISA manager will be able to tell you how much you can transfer.

# How many and how much ....?

## *How many ISAs can I have?*

You can hold as many ISAs as you want, but you can only put money into **either** one Maxi ISA **or** up to three Mini ISAs - one each for cash, stocks and shares and life insurance, in any one tax year

You cannot put money, for example, into both a Maxi ISA and a Mini ISA in the same tax year, or into two Mini cash ISAs.

You may also be able to put money into a TESSA only ISA if you have a TESSA that has matured. See page 22 for more detailed information about this.

## *How much money can I put into ISAs?*

In each of the tax years 2001/2002 to 2005/2006 you can put in up to £7,000 in total (plus any capital sum from a matured TESSA - see page 22). You can then put in up to £5,000 in each subsequent tax year from 2006/2007. A tax year runs from 6 April to 5 April the following year.

Each year the money can be put into either

| | **2001 - 2006** | **Later years** |
|---|---|---|
| **one Maxi ISA** | total £7,000 | total £5,000 |
| of which these amounts can be put into | | |
| stocks and shares | up to £7,000 | up to £5,000 |
| cash | up to £3,000 | up to £1,000 |
| life insurance | up to £1,000 | up to £1,000 |
| **or Mini ISAs for** | | |
| stocks and shares | up to £3,000 | up to £3,000 |
| cash and | up to £3,000 | up to £1,000 |
| life insurance | up to £1,000 | up to £1,000 |

**Remember, you can only put money into either one Maxi ISA or up to three Mini ISAs (one for each type of saving) in each tax year**.

Turn to pages 17 and 18 for more detailed information on limits.

# What happens if ...?

## *... I change my mind?*

ISA managers offering some kinds of ISA may give you a 'cooling off' or cancellation period (usually 7 or 14 days), in which you can change your mind about buying. If you change your mind within that time you will be free to put money into an alternative ISA in the same tax year with the same or a different manager.

If you change your mind after that time, or in a case where there is no cancellation or cooling off period, you will still count as having put money into that ISA, and your choice of a new ISA will be restricted in the same tax year.  However, you could transfer the existing ISA to another ISA manager.

## *... I want to take my money out?*

You can take your money out at any time, without losing any tax benefits you have already built up. However, some ISAs may run for a fixed period or require notice of withdrawal, and you may lose some interest or a bonus if you withdraw early. In some cases there may also be a penalty if you surrender an ISA life insurance policy early.

With a stocks and shares or life insurance ISA you may not get back all the money you put in, particularly if you withdraw during the early years of an investment.

If you take money out, any that you put back later will count against the ISA limits for the year.

**Example**
Denise opens a cash mini ISA with the sum of £2,500. A few weeks later she withdraws £2,000. Later on in the same year Denise decides to replace the money by putting new funds into the account. However she is only able to replace £500. This is because the annual subscription limit for a cash mini ISA account is £3,000 in each tax year, and Denise has already put in £2,500 when she first opened the account.

## *... I want to change the savings and investments in my ISA?*

You can switch from one savings product or investment to another at any time within the same component, but a particular ISA may only allow certain savings or investments. If you want to include savings and investments that are not available for your ISA, you may have to transfer to another manager.

## *... I have a complaint?*

The first step is to take it up with your ISA manager. They will have a complaints procedure, which should be able to help you.

If you are not happy with the answer you get, you can take the matter up with the Financial Ombudsman Service. The Ombudsman Service aims to resolve individual disputes between consumers and financial firms. The Ombudsman Service is free for consumers and is an informal alternative to the courts. You can call the Ombudsman Service on **0845 080 1800** (calls are charged at local rates).

## *... I pay into too many ISAs?*

If, by mistake, you put money into more than one Maxi ISA, into a Maxi and a Mini ISA, or into more than one Mini ISA of the same type in the same tax year, then the payment into the second ISA is invalid, and you are not entitled to any tax relief on investments held in the second ISA.

**Note**: You must tell the manager of the second ISA as soon as possible that it is invalid. You cannot correct this mistake by closing the first ISA. If you are unsure about what to do call the Inland Revenue helpline on **0845 604 1701** for advice (calls charged at local rates).

## *... I go abroad?*

If you start an ISA in the UK and then go abroad, you cannot carry on putting money into the ISA (unless you are a Crown employee working overseas or the husband or wife of one of these people). However, you can keep your ISA and you will still get tax relief on investments held in the ISA. When you return you can start putting money in again (subject to the normal annual limits).

## *... I die?*

Your ISA will end on the date of your death. There will be no tax to pay on income or capital gains up to that date, but your personal representatives will have to account for tax on any income or gains arising after your death.

The ISA manager will either sell the investments and pay the proceeds to your personal representatives (or a beneficiary of your estate) or transfer the investments directly into their hands. The terms and conditions of the ISA may specify which it will be.

An ISA life insurance policy will pay out on your death. Your personal representatives will have to claim the death benefit. There will be no tax to pay on income or capital gains which arise before the insurer accepts the claim. However, your personal representatives will be taxed on any interest that is paid if there is then a delay in paying out the claim. The insurer will deduct tax at the lower rate before paying over the interest.

ISA investments form part of your estate for Inheritance Tax purposes.

## What are the tax benefits?

- You pay no tax on any of the income from your ISA savings and investments. This includes dividends, interest and bonuses.
- You pay no tax on capital gains arising on your ISA investments (but note that this means that losses on ISA investments cannot be allowed for Capital Gains Tax purposes against capital gains outside your ISA).
- Your ISA manager will arrange for tax credits attached to dividends from UK companies (which since April 1999 have had a value of 10 per cent) to be paid into your ISA until 5 April 2004. Dividends from companies based outside the UK do not carry a tax credit.
- The insurer does not have to pay tax on income and capital gains on investments (including claiming tax credits on dividends from UK companies) used to back your ISA life insurance policies. You do not have to pay any tax when the policy pays out.
- You can take your money out at any time without losing tax relief.
- You do not have to declare income and capital gains from ISA savings and investments - or even tell your Tax Office that you have an ISA.

## Other questions

### *I am under the age of 18 - can I take out an ISA ?*

If you are aged 16 or 17 you can take out a cash ISA. This can be either a mini cash ISA or a maxi ISA where you can only put money into the cash component. The subscription limits are the same as for savers who are over 18, so you can subscribe up to £3,000 in each tax year.

If you are aged 15 or under, you cannot take out an ISA.

### *Can I put money into my 16 or 17 year-old child's ISA ?*

ISAs for 16 and 17 year-olds are intended primarily for those in full or part-time employment, including those still at school with, for example, Saturday jobs, but ISAs will also be used by some young people to save money given to them by their parents. If you give your child money to invest into an ISA account, and the total

investment income arising on all gifts from you, not just in ISAs, exceeds £100 in any tax year, all the income arising will be treated as part of your income for that tax year for income tax purposes. You should report that income to your Tax Office.

This rule does not prevent you from giving your child money to invest in an ISA - you just have to take care not to give your children too much. The £100 income limit for each child applies to each parent, not to both taken together.

## *I am 17 and have a cash ISA - what happens when I reach the age of 18 ?*

If you have put money into a mini cash ISA in the tax year in which you reach 18, you can go on doing so on and after your 18th birthday, subject to the normal limit. Once you have reached 18 you can also apply to open a stocks and shares Mini ISA and/or an insurance Mini ISA for that tax year, and will have to complete a new application for either of those, in the same way as any other investor.

If you have been putting money into the cash component of a maxi ISA in the tax year in which you reach 18, you can go on doing so on and after your 18th birthday, subject to the normal limit. Once you have reached 18, you can also put money into the stocks and shares and insurance components of your Maxi ISA. In any of these situations you will not have to complete a new application.

Remember that you cannot put money into a cash mini ISA and a maxi ISA in the same tax year.

## *What about employee share schemes and ISAs ?*

If you are in an Inland Revenue approved all-employee share scheme run by your employer, that is, a savings related share option - 'Sharesave' - or profit sharing scheme or the new Share Incentive Plan, then you can transfer any shares you get from that scheme into the stocks and shares component of an ISA without having to pay Capital Gains Tax, provided your ISA manager agrees to take them.

The value of the shares at the date of transfer counts towards the annual limit. This means you can transfer up to £7,000 - worth of shares in each of the tax years 2001/2002 to 2005/2006, or £5,000 in any later year from 2006/2007 (assuming that you make no other payments to ISAs, except a TESSA-only ISA, in those years).

**Remember that if you want to transfer more than £3,000-worth of shares you must have a Maxi ISA. See page 18 for further details.**

The shares must be transferred within 90 days from the day they emerge from the scheme (or, in the case of an approved profit sharing scheme, from the third anniversary of the date the shares were given to you, if earlier).

Your employer should be able to tell you more.

## *Can I put windfall shares into my ISA ?*

No. You can only transfer shares you own into an ISA if they have come from an employee share scheme of the kinds shown on page 12. Otherwise shares must be purchased by the ISA manager in the open market.

The situation is the same if you have shares that you have inherited. You are not able to transfer them into an ISA.

## *Can I use an ISA to back a mortgage?*

Yes, the proceeds from ISA investments can be used for any purpose, but you should discuss the implications with your financial adviser or mortgage lender.

## *Can I get reports and accounts of the companies in my stocks and shares ISA?*

Yes. Your ISA manager can arrange for you to receive reports and accounts, although there may be a charge. You may also be able to attend and vote at the annual meeting of companies in which your ISA invests.

# Some Points In More Detail

## The CAT Standards

There are different CAT standards for cash, stocks and shares and life insurance ISA investments.

### *The standard for cash ISAs*

| | |
|---|---|
| Charges | • There must be no one-off or regular charges of any kind, such as charges for withdrawals or for any regular service (such as use of cash machines). Charges for replacements (such as duplicate statements or lost cards) are permitted, however. |
| Access | • The minimum transaction must be no greater than £10. |
| | • Savers must be able to withdraw their money within seven working days or less. |
| Terms | • The interest rate must be no lower than two percentage points below base rate. |
| | • Upward interest rate changes must reflect base rate movements within a calendar month. Downward changes may be slower. |
| | • There must be no other conditions (such as limits on frequency of withdrawals). |

## *The standard for stocks and shares ISAs*

| | |
|---|---|
| Charges | • The total charge must be no more than 1 per cent of net asset value per year. |
| | • There must be no other charges to be paid by the saver. |
| Access | • You must be able to put in amounts as small as £500 for a lump sum or £50 a month for regular savings. |
| Terms | • Investment may be in authorised unit and investment trusts or in open-ended investment companies. |
| | • A fund must be at least 50 per cent invested in ISA-qualifying shares and securities that are listed on European Union stock exchanges. |
| | • Units and shares must be single priced (that is, no separate buying and selling prices). |
| | • The investment risk must be highlighted in product literature. |

A CAT standard stocks and shares ISA may hold units or shares in one or more funds which meet these requirements. If holding them in the ISA entails any additional features (such as additional charges) these should be taken into account in deciding whether the ISA meets the standard.

## *The standard for life insurance ISAs*

| | |
|---|---|
| Charges | • The annual charge must be no more than 3 per cent of the value of the fund. |
| | • There must be no other charges (such as a separate charge for the guarantee on surrender values). |
| Access | • The minimum premium must be no more than £25 a month for regular savings, or a £250 lump sum. |
| Terms | • Surrender values should reflect, over time, the value of the underlying assets of the fund. |
| | • There must be no specific surrender penalties. |

- Three years after paying a premium, and thereafter, the surrender value should at least return the value of the premium.

A CAT standard life insurance ISA may hold one or more life insurance policies. If holding them in the ISA entails any additional features (such as additional charges) these should be taken into account in deciding whether the ISA meets the standard.

A CAT standard life insurance ISA may permit lump-sum savings, regular savings, intermittent savings or any combination of these. The surrender value guarantee applies separately to each premium payment.

## Savings and investments that can be included in ISAs

### *The cash component can include*

- bank and building society accounts
- units or shares in UK authorised unit trusts and open-ended investment companies (oeics) which are money market schemes (sometimes called 'cash funds') and fund of funds schemes which invest in them
- National Savings products which are specially designed for ISAs (but not other National Savings products such as the Investment Account, Savings Certificates or Pensioners' Guaranteed Income Bonds).

### *The stocks and shares component can include*

- shares and corporate bonds issued by companies listed on a recognised stock exchange anywhere in the world
- gilt edged securities ('gilts'), similar securities issued by governments of other countries in the European Economic Area and 'strips' of all these securities
- units or shares in UK authorised unit trusts or open ended investment companies (oeics) which invest in shares and securities (called securities schemes and warrant schemes) and fund of funds schemes which invest in them
- shares and securities in approved investment trusts (except property investment trusts)

- units or shares in Undertakings for Collective Investment in Transferable Securities (UCITS) funds based elsewhere in the European Union (these are similar to the UK authorised unit trusts and OEICS listed above)

- any shares which have been transferred from an Inland Revenue approved all-employee scheme under the special rules described on page 12.

These investments must meet certain conditions to qualify for ISAs. ISA managers will be able to tell you which ones can be included in their own ISAs.

## *The life insurance component can include*

- 'unit linked' or 'investment linked' policies. This is like a 'pooled' investment such as a unit trust

- 'with profits' policies. This is a more traditional type of life insurance policy where you participate in the profits the insurer makes from investing your premiums through 'bonuses' which the insurer declares, usually once a year.

**Note**: The life insurance component can include only certain life insurance policies on the saver's own life, which are specially designed for ISAs. These may be the ISA manager's own policies, or the ISA manager may offer a range of policies from different insurers.

ISA policies must meet a number of conditions to qualify. Managers of life insurance ISAs will be able to give you details of their own policies.

## *A note on holding cash in the stocks and shares and life insurance components*

Cash may only be held in the stocks and shares and life insurance components of ISAs for the purpose of investing in qualifying stocks and shares or life insurance policies. This includes cash subscriptions, interest and dividends, and proceeds from disposals of qualifying investments which have not yet been reinvested.

The ISA manager may pay interest on this cash while it is held in the account. There is no income tax to pay on this interest, but the manager is required by law to deduct a flat rate 20 per cent charge before crediting it to the account. You do not have to declare this interest on a tax return.

# The choice between Maxi or Mini

You can put money into any of the three components of a Maxi ISA. If you do not put the maximum allowed into the cash or life insurance components (where they are offered by the Maxi ISA), you can put the excess into the stocks and shares component.

With Mini ISAs the limits are fixed. This means that even if you put nothing into, say, a cash Mini ISA during the year, you could still only put £3,000 into, say, a stocks and shares Mini ISA.

This table shows how many ISAs you can have and how much money you can put into each.

| Your options in a tax year | Total investment allowed in each tax year 2001/2002 to 2005/2006 | Total investment allowed in subsequent tax years from 2006/2007 | Maxi or Mini? |
|---|---|---|---|
| One Maxi ISA | Up to £7,000 but no more than £3,000 in cash and £1,000 in life insurance | Up to £5,000 but no more than £1,000 in cash and £1,000 in life insurance | You should always choose a Maxi ISA if you want to invest more than £3,000 in stocks and shares |
| Up to three Mini ISAs | • Up to £3,000 in a stocks and shares ISA<br>• £3,000 in a cash ISA<br>• £1,000 in a life insurance ISA | • Up to £3,000 in a stocks and shares ISA<br>• £1,000 in a cash ISA<br>• £1,000 in a life insurance ISA | You should always choose Mini ISAs if you want different managers to manage your different kinds of savings |

Remember, you can also put any money you paid into a maturing TESSA into a cash Mini ISA or into the cash component of a Maxi ISA or into a TESSA only ISA. (see page 22 )

Whether you choose a Maxi or a Mini ISA in any year is up to you, but remember

- if you want to invest more than £3,000 in stocks and shares, you must open a Maxi ISA
- if you want different ISA managers for different kinds of saving, you will need Mini ISAs
- always shop around for the arrangement that will give you the best deal or is most convenient.

## TESSAs (Tax Exempt Special Savings Accounts)

A TESSA is a special bank or building society account that offers tax-free interest provided the account is maintained for a fixed period of five years. So as long as you leave your savings in the account over that period any interest, dividends or bonus earned will be totally free of tax.

TESSAs have been replaced by cash ISAs and no new TESSAs could be opened after 5 April 1999. TESSAs opened by that date can continue to run to maturity under the normal TESSA rules.

The information that follows is for savers who already have TESSAs.

### *How much can be saved in a TESSA?*

Up to £9,000 in total can be saved in a TESSA over five years, but there are limits to the amount that can be deposited each year. Up to £3,000 could be deposited in the first year and no more than £1,800 in each later year. Each TESSA year begins on the anniversary of the date the account was opened.

**Example**

| Year | Amount deposited £ |
|---|---|
| 1 | 3,000 |
| 2 | 1,800 |
| 3 | 1,800 |
| 4 | 1,800 |
| 5 | 600 |
| **Total** | **9,000** |

In this example you cannot deposit more than £600 in year five because of the £9,000 overall limit.

There were special rules for **follow up TESSAs**. These TESSAs were opened after an earlier TESSA had matured. Under these special rules, the first year deposit limit was £3,000 or the amount deposited in the earlier TESSA (up to £9,000, but excluding interest or bonuses) if this was greater. The deposit limits of £1,800 in later years, and the overall deposit limit of £9,000 over the five years, are the same for any other TESSA.

## *When can I deposit money in a TESSA?*

You may deposit money in your TESSA as often as you like, but once you reach the yearly deposit limit you must wait until the next year before you can deposit any more.

## *If I do not deposit the full amount in any year can I make it up later?*

If you do not deposit the full amount in any year, you cannot carry the difference forward to a later year. You can only make up the shortfall within the normal annual limit of £1,800.

## *Can I withdraw any money from my TESSA before the five years are up?*

Yes. You can withdraw some of the interest (but the bank or building society must retain a sum representing the income tax that would be due on a normal taxable account (20%)). This sum is not paid over to the Inland Revenue, but stays in the account until the end of the five years. You can then withdraw it without losing the tax exemption.

**Example**
Andy deposited £1,000 in a TESSA on 5 April 1999. If the bank or building society pays interest at 5% he will get £50 interest in a year. The maximum amount Andy can withdraw without losing the tax exemption is £40. This is calculated as follows.

| | **£** |
|---|---|
| Interest credited | 50 |
| less tax at the lower rate (20%) | -10 |
| | |
| The maximum amount Andy may withdraw | 40 |

The sum remaining in the account is £1,000 + £10 = **£1,010**

## *Can I withdraw interest at any time in the five years?*

Yes, if the bank or building society's TESSA terms and conditions allow withdrawals. You can withdraw as much of the interest (less the amount representing income tax) as you like at any time without losing the tax exemption. You can withdraw all the money deposited, and all the interest tax-free, at the end of the five years.

## *Can the account lose its TESSA status?*

The account will cease to be a TESSA if you

- close the account before the end of the five-year term
- deposit more than is allowed in any year
- withdraw any of the money you deposited before the five years are up
- withdraw too much interest before the five years are up.

If you do any of these things, then the account will cease to be a TESSA and it will lose its tax-exempt status.

## *What happens if the account ceases to be a TESSA?*

If the account ceases to be a TESSA, all the interest earned is taxable in the year it ceases. The bank or building society will deduct tax from the interest at 20%. If you pay tax at the higher rate of 40%, you will have some further tax to pay on the interest.

## *Must I include this interest in my tax return?*

Yes, if the account loses its tax-exempt status you must include the interest in your Tax return, if you receive one. If you do not get a Tax Return, and you are liable to pay tax at the higher rate, you must tell your Tax Office.

## *What if I do not pay tax or pay tax at the starting rate?*

If you are not liable to pay tax or if you pay tax at the starting rate of 10%, you may be able to claim back some or all of the tax deducted. Our booklet IR110 'A guide for people with savings' gives more information on how to claim - see page 27 for details of how to obtain this booklet.

### *What happens if I die before the end of the five-year period?*

No tax will be charged on the interest paid up to the date of your death, but the account cannot continue as a TESSA after that date and any interest paid after that date will be taxable.

## Transferring a TESSA

### *Can I move my TESSA to a different bank or building society during the five years?*

Yes, but to keep the tax exemption, you must ask the new bank or building society to transfer the account for you. If you try to move the account by withdrawing any money you will break the rule that the money deposited must remain in the account. That will mean all the interest earned will be taxed.

Your current bank or building society cannot refuse to transfer your TESSA to a different bank or building society. However, their terms and conditions may mean you lose some interest or bonuses if you do. Banks and building societies are not obliged to accept transfers to them.

### *What happens after five years when my TESSA matures?*

All the interest and bonuses earned up to that date are tax-free and you can withdraw the money without restriction. At maturity the account ceases to be a TESSA and any further interest and bonuses are taxable in the normal way.

### *Can I transfer my TESSA money into an ISA?*

Yes. Once your TESSA has matured you can choose to transfer the money you deposited in the TESSA (but not interest or bonuses) into the cash component of an ISA. This is **on top** of your normal annual ISA limits. You can transfer the money from your TESSA into

- the cash component of a new or existing Maxi ISA
- a new or existing cash Mini ISA, or
- a special ISA, called a TESSA-only ISA, which is set up solely to receive money from a matured TESSA.

You must do this within **six months** of the date the TESSA matures.

## *Does the ISA have to be with the same bank or building society?*

No. You can use any ISA manager who offers a TESSA only ISA, a cash mini ISA or the cash component of a maxi ISA.

If the TESSA and the ISA are managed by the same bank or building society they will know how much you can transfer. If your new ISA manager is not the same as your TESSA provider, then the ISA manager will ask you to obtain from your TESSA provider a maturity certificate showing the date of maturity of the TESSA, and the amount you deposited.

## *Do I have to transfer the whole amount?*

No, you can put in as much or as little as you like, but you cannot put in more than the amount you deposited in your matured TESSA, excluding interest or bonuses.

## *What about the interest from the TESSA?*

Interest and bonuses from the matured TESSA can be subscribed to any ISA (except a TESSA only ISA) within the annual ISA limits.

# PEPS (Personal Equity Plans)

A PEP is a way of investing in certain kinds of shares and securities tax-free.

PEPs have been replaced by stocks and shares ISAs from 6 April 1999 and no new subscriptions to PEPs could be made after that date. Existing PEPs at that date can remain in existence. The information that follows is for those investors who have existing PEPs.

The rules for PEPs changed from 6 April 2001 to bring them more in line with the rules for stocks and shares ISAs.

## *What are the tax benefits?*

These are the same as for stocks and shares ISAs.

- You pay no tax on any of the income from your PEP investments.

- You pay no tax on capital gains arising on your PEP investments (but note that this means that losses on PEP investments cannot be allowed for Capital Gains Tax purposes against capital gains outside your PEP).

- Your PEP plan manager will arrange for tax credits attached to dividends from UK companies (which from April 1999 have had a value of 10 per cent) to be paid into your PEP until 5 April 2004. Dividends from companies based outside the UK do not carry a tax credit.

- You can take your money out at any time without losing tax relief.

- You do not have to declare income and capital gains from PEP investments, or tell your Tax Office that you have a PEP.

## *How does a PEP work?*

All PEPs are managed by a plan manager under terms agreed with you in writing. You can no longer pay money into a PEP, but the plan manager continues to manage the investments made from funds you subscribed before 6 April 1999.

All PEP plan managers must be approved by the Inland Revenue and authorised by the Financial Services Authority, but neither they nor any other Government Department have approved any PEPs. They do not guarantee that any PEP plan

manager is able to manage any PEP satisfactorily, or that any PEP investment will produce the expected return.

## *Changes from 6 April 2001*

- The difference between single company PEPs and general PEPs has been removed. This means that all PEPs are now subject to the same rules.
- The investments which can be held in a PEP now follow the rules for stocks and shares ISAs (see page 16). This means that PEPs can now invest in the listed shares of companies based anywhere in the world.
- Subject to the plan manager's terms and conditions you can now transfer part of a PEP to a different manager, not just a whole PEP as before. The rules are the same as for transfers of ISAs (see page 7).

## *What has not changed?*

- Any investments held at April 2001 which would have been eligible under the former PEP rules, but are not eligible under the ISA rules, can continue to be held in a PEP. However, you cannot add to any existing PEP investment unless it qualifies under the new rules.
- The treatment of interest paid on cash held awaiting investment has not changed - see below.

## *When can I take money out of my PEP?*

You can receive income from the investments held in a PEP, take money out of, or close the PEP at any time without losing any tax relief you have already built up. However, once you have taken money out, you cannot put it back in.

## *Can I hold cash in a PEP?*

Yes, but only for the purpose of purchasing investments.

## *What about interest on cash held in a PEP?*

Interest on cash held in a PEP whilst awaiting purchase of investments will be credited without deducting tax.

If you withdraw interest paid on cash (not investments) held in your PEP, this interest is not taxable unless you withdraw more than £180 in a tax year. If you withdraw more than £180 then all such interest withdrawn in the tax year is subject to tax. The plan manager will deduct tax at 20%. Higher rate taxpayers will have to pay further tax on this interest. You must declare this interest on your Tax Return or if you do not get a Tax Return and you are liable to tax at the higher rate you must tell your Tax Office. If you are not liable to tax on the whole of this interest, you will be able to claim back some or all of the tax deducted.

## *Can I get reports and accounts of the companies in my PEP?*

Yes, Your PEP plan manager can arrange for you to receive reports and accounts, although there may be a charge. You may also be able to attend and vote at the annual meeting of companies in which your PEP invests.

## *What happens if I go abroad?*

You do not have to close your PEP and the income and gains will continue to be exempt from UK tax.

## *What happens if I die?*

The PEP will end on the date of your death. There will be no tax to pay on income or capital gains up to that date, but your personal representatives will have to account for tax on any income or gains arising after your death. The plan manager will either sell the investments and pay the proceeds to your personal representatives (or a beneficiary of your estate) or transfer the investments directly into their hands, as specified by the terms and conditions of the PEP.

PEP investments form part of your estate for Inheritance Tax purposes.

# Getting more help and advice

If you have any general questions about the tax rules for ISAs, TESSAs and PEPs that this leaflet does not cover, you can call the Inland Revenue ISA Helpline on **0845 604 1701** between 8.30am and 5.00pm Monday to Thursday and between 8.30am and 4.30pm on Friday (calls are charged at local rates).

Further information is also available on the Internet at **www.inlandrevenue.gov.uk**.

We can provide you with factual information about ISAs, but we cannot advise you on whether you should open an ISA, or about particular ISA products. An authorised financial adviser, or the ISA manager concerned, can help you with individual advice.

Copies of booklet IR110 'A guide for people with savings' are available from any Inland Revenue Office (see your telephone book under 'Inland Revenue') or on the Internet at **www.inlandrevenue.gov.uk**

The Financial Services Authority (FSA) regulates financial services and protects consumers. The FSA can tell you if a firm is authorised, and can help you if you have a complaint and are unsure whom to contact. However, it cannot recommend firms or advisers, or tell you whether a particular investment is right for you.

The FSA also has a wide range of user-friendly booklets and factsheets. These are available from the FSA Consumer Helpline on **0845 606 1234** (calls are charged at local rates) or from its website at **www.fsa.gov.uk/consumer**.

The FSA website contains ISA Comparative Tables. These let you compare stocks and shares ISAs based on unit trusts and open-ended investment companies from different ISA managers.

# Our service commitment to you

**The Inland Revenue and Customs and Excise are committed to giving you the best service we can by**

## *acting fairly and impartially*

We
- treat your affairs in strict confidence, within the law
- want you to pay or receive only the right amount due.

## *communicating effectively with you*

We aim to provide
- clear and simple forms and guidance
- accurate and complete information.

## *providing good quality service*

We aim to
- handle your affairs promptly and accurately
- be accessible
- keep your costs to the minimum
- help customers with special needs
- be courteous and professional.

## *taking responsibility for our service*

We
- publish our customer service aims and achievements annually
- want to hear from you if you wish to comment, or complain, so we can improve our service. We advise you how to do this.

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## *We can provide better service if you help us by*

- keeping accurate and up-to-date records
- letting us know if your personal or business circumstances change
- giving us correct and complete information
- paying on time.

Further information on customer service is available at Inland Revenue and Customs and Excise local offices, set out in our Charters, complaint leaflets and Codes of Practice.

These notes are for guidance only and reflect the tax position at the time of writing.
They do not affect any right of appeal.

Issued by Inland Revenue Marketing and Communication
January 2002
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Printed by The Astron Group 01/02 NSV Code R2P 3190