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FEATURE ARTICLE

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NISAs – Legitimate Tax Avoidance for Middle Britain

When considering New Individual Savings Accounts (NISAs) the first thing to stress is that they are not an investment in their own right. The best way to think of a NISA (which replaced ISAs in July 2014) is that it is a "box" or "wrapper" in which an individual can shelter savings and investments from tax. This is because for assets held within a NISA you pay no capital gains tax and no further tax on income or interest. For certain investments where income tax has been deducted "at source" this means that tax can be reclaimed by the NISA manager although this does not apply to, for example, the tax credit applying to UK dividends. It does however apply to interest paying investments. It is also worth noting that the tax wrapper status of NISAs are generally advantageous but may in certain instances be disadvantageous. An example would be that if a capital loss is made within a NISA that capital loss cannot potentially be set-off against gains made outside of a NISA to reduce a CGT liability whereas it might have been available for that purpose if outside of a NISA.

All existing ISAs became NISAs on the 1st July 2014 and NISAs are available to any UK resident (or a Crown servant e.g. diplomatic or overseas civil service, or their spouse or civil partner who don't live in the UK) aged 18 or over and 16 or over for just cash NISAs. (From 1st July 2014, savers aged 16 to 18 have been able to subscribe up to the £15,000 limit to a Cash NISA, but are unable to open a NISA stocks and shares account. They can however in addition invest up to £4,000 in a Junior ISA which can be held in a Cash Junior ISA or a Stocks and Shares Junior ISA or any combination of the two up to the £4,000 limit.) There is no upper age limit for a NISA and a NISA can only be arranged on an individual basis (so it cannot be held jointly) and it cannot be held in a trust.

With reference to Junior ISAs the money belongs to the child who can take control of the account when they're 16, but can't withdraw the money until they turn 18.

Under rules which came into effect on 1st July 2014 you can split the NISA allowance (£15,000 for the tax year 2014/15) as you wish between a Cash NISA and a Stocks and Shares NISA. You can withdraw your NISA subscription whenever you wish, although once withdrawn you can't put this money back into a NISA without it counting as a new subscription. Investment limits increase each tax year in line with inflation, as measured by the consumer prices index (CPI). In his Autumn Statement on 3rd December 2014 the Chancellor confirmed that from April 2015, the NISA allowance will rise to £15,240 and the Junior ISA limit will increase to £4,080.

Radical Changes:

In July 2014 there were the most radical changes to ISAs since they were introduced in 1999 (hence the change in name to NISAs). These included, for example:

- ✓ Improved Flexibility: An individual can split the NISA allowance as they wish between a Cash NISA and a Stocks and Shares NSA up to the new annual limit in total.
- ✓ Improved transfer options: It is now possible to transfer from a Stocks and Shares NISA to a Cash NISA and vice versa. (Under previous rules you could only transfer from a Cash ISA to a Stocks and Shares ISA.)
- ✓ Tax free interest in Stocks and Shares NISA: You have always been able to hold cash in a Stocks & Shares ISA, but any interest was in effect paid net of basic rate tax. Under the new rules interest on cash held in a Stocks and Shares NISA is completely tax-free.
- ✓ New permitted investments: The rules on what can be held in a NISA were relaxed so that, for example, certain securities, such as retail bonds which have less than 5 years to run to maturity at the time they are first held in a NISA can now be held. (The Government is also consulting on allowing peer to peer loans to be eligible for NISAs, but as I write this article that consultation has not finished.)

IHT and NISAs:

One particular area of interest for tax planning was that on 5th August 2013 the Treasury introduced new rules to allow investors to hold shares in small companies listed on the Alternative Investment Market (AiM) in ISAs (now NISAs). This means that in many cases investors in AiM shares will now get a double tax break because the Government confirmed that when AiM and similar shares are held in a NISA, the normal inheritance tax (IHT) business property relief (BPR) rules apply.

NISA investments are tax efficient for as long as they are held, but are normally counted as part of the investor's estate on death and may generate an inheritance tax liability. Many AiM shares qualify for business property relief, which takes them out of the inheritance tax net if they have been held for at least two years. (Please note that property development and investment business AiM companies do not typically qualify for business property relief.)

It should be noted that AiM stocks can be notoriously volatile and potentially illiquid and investors should not choose investments based solely on their tax benefits.

Finally, in the Autumn Statement in 2014 the Chancellor announced that new rules were being introduced allowing the tax advantages of married NISA savers to be inherited by a surviving spouse or civil partner on the death of the NISA holder. According to the Government 150,000 married NISA savers pass away each year, and their NISA tax advantages die with them, even if they were saving as a couple. It was confirmed that from 3rd December 2014 the surviving spouse/civil partner of those who died on or after that date will benefit from a one-off NISA allowance equal to the total amount the deceased held in their NISA(s) at the date of death and this additional allowance will be available to the surviving spouse/civil partner from 6th April 2015. (Surviving spouses/civil partners will in addition have their usual 2015/16 NISA allowance available.)

Unfortunately as I write this article the full details of how this will work in practice and the full rules are still subject to Consultation but it is important to note that as it stands from the date of death of the spouse/civil partner the NISA wrapper of the deceased is lost and the underlying assets become potentially subject to income tax on any interest or dividend income generated or capital gains tax where gains are made. In addition the value of the deceased individuals NISA(s) are potentially subject to inheritance tax on death with the one main exception already discussed - where NISA investments qualify for business property relief such as qualifying AiM shares held for a two year period. However it is important to remember that transfers of any assets between spouses on death are IHT free.

Questions which need to be answered by the Consultation include for example whether the additional NISA allowance has to be with the same NISA manager as the deceased, and whether assets can be transferred into the new NISA "in-specie" and what happens if those assets have increased in value between the date of death and the granting of probate/opening of the new NISA?.

Conclusion:

Unfortunately it will not simply a case of transferring a NISA wrapper from one person to another but of NISA(s) in one name ceasing to exist and a new NISA(s) having to be opened and the actual process could ultimately be quite complicated and involve a period when assets are potentially taxable. But then as I always say investment is ultimately simple but not necessarily easy.

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