Canada Life

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Investment Bond Briefing Note 1

Briefing Note

This briefing note has been written for professional adviser use only

Taking money from a bond: sub-policy surrender or partial surrender?

Canada Life investment bonds offer the facility to divide the premium into a series of identical policies.

This means that clients wishing to withdraw part of their investment have a choice as to how to take it, either by taking a withdrawal or by surrendering individual policies.

Which way is best will depend on the client's circumstances at the time. Before deciding which option is suitable there are a number of factors to take into consideration, but investment bonds should always be segmented so that the choice can be made.

One of the main benefits of an investment bond is tax deferral, so this note assumes that the objective of the exercise is to generate the minimum chargeable gain possible at the time of the event.

Any withdrawal will be taken into account on the eventual full surrender or maturity of an investment bond or the death of the last surviving life assured.

1. Will the bond charging structure compromise the decision?

Not with the CanInvest Select Account, as there are no penalties provided that you leave £250 in the bond.

Similar rules apply, with different minima, for the international bonds available through our Isle of Man and Dublin offices.

2. Apart from the chargeable event, what other considerations are there?

There are two main ones: the timing of the chargeable event and the future 5% withdrawal allowance.

Firstly, chargeable gains in respect of withdrawals are calculated at the end of the policy year, whereas gains on policy surrenders are calculated on the actual date of the event.

It is common for these dates to fall into different tax years, which may mean that the tax bill is payable earlier. Also, if the client has fluctuating income the timing of the chargeable event may be crucial.

As regards future 5% withdrawals, if a full policy surrender is used the encashment of policies means that the 5% withdrawal will not be available on those policies in future.

For example, if a client starts with 100 individual policies of £1,000 each and surrenders 20 individual policies, their 5% tax deferred withdrawal allowance will drop from £5,000 each year to £4,000.

Also, any 5% withdrawal allowance carried forward and not used in respect of previous years for the policies surrendered will be lost.

3. So which is best, a withdrawal or policy surrender?

It is truly 'horses for courses' and depends on the client's circumstances. As a general rule, if the amount required is less than the 5% withdrawal allowance, use that.

If the amount required is much higher than the 5% withdrawal allowance, or regular withdrawals have used it up, policy surrenders would normally be best.

Do not think that just because the client is a basic rate taxpayer that the chargeable gain can just be ignored. It could be the case that when the top-slice gain is added to the client's other taxable income, the total will exceed the higher rate threshold.

Examples

a. 5% withdrawal covers the amount required

Bond commenced	01/05/2008
Premium	£100,000
Policies	100 at £1,000 each
Withdrawals to date	nil
Partial surrender required	£40,000 on 01/11/17
Current surrender value	£160,000 (£1,600 each policy)

Partial withdrawal

5% allowance	50% (including current policy year)
Allowance	£50,000
Partial surrender	£40,000
Chargeable gain	nil
Date of chargeable event	not applicable

Individual policy surrender

Amount required	£40,000
Number of policies encashed	25
Gain for each policy	£600
Chargeable gain	£15,000
Date of chargeable event	01/11/17
Top slice	£1,667
Tax year	2017/18

5% allowance now only £3,750 a year

b. Large partial surrender in year two

Bond commenced	01/05/2016
Premium	£100,000
Policies	100 at £1,000 each
Withdrawals to date	nil
Partial surrender required	£72,600 on 01/11/17
Current surrender value	£110,000 (£1,100 each policy)

Partial withdrawal

5% allowance	10% (including current policy year)
Allowance	£10,000
Partial surrender	£72,600
Chargeable gain	£62,600
Date of chargeable event	30/04/18
Top slice	£31,300
Tax year	2018/19

Individual policy surrender

Amount required	£72,600
Number of policies encashed	66
Gain for each policy	£100
Chargeable gain	£6,600
Date of chargeable event	01/11/17
Top slice	£6,600
Tax year	2017/18

5% allowance now only £1,700 a year

c. 5% withdrawal used up

Bond commenced	01/05/2013
Premium	£100,000
Policies	100 at £1,000 each
Withdrawals to date	Year 1 & 2 £5,000 (taken in July each year) Year 3 £6,000 taken in July (1,000 chargeable gain 30/04/16) Year 4 & 5 £5,000 (taken in July each year)
Partial surrender required	£38,000 on 01/11/17
Current surrender value	£95,000 (£950 each policy)

Partial withdrawal

5% allowance	0% (fully used)
Allowance	nil
Amount required	£38,000
Chargeable gain	£38,000
Date of chargeable event	30/04/18
Top-slice	£19,000
Tax year	2018/19

Individual policy surrender

Amount required	£38,000
Number of policies encashed	40
Gain per policy	£200*
Chargeable gain	£8,000
Date of chargeable event	01/11/17
Top slice	£2,000
Tax year	2017/18

5% allowance now only £3,000 per year

*This gain arises because the calculation on a policy surrender takes into account the previous withdrawals on each policy.

And whilst not wishing to complicate matters further, in some cases the lowest chargeable gain figure can be achieved by taking a combination of withdrawal and policy surrender.

The information regarding taxation is based on our understanding of current legislation, which may be altered and depends on the individual circumstances of the investor. We recommend that investors seek professional tax advice.

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