STERLING

Tax guide

This guide aims to help you understand the tax treatment of the Sterling Investment Bond, Sterling Individual Savings Account, and Sterling Investment Account. If you are reading it without an adviser, we recommend you take financial advice.

Please consider all the tax implications when taking out, making changes to, and disposing of some or all of your investment.

We have based this guide on our understanding of current UK law and HM Revenue & Customs (HMRC) practice as at April 2018.

The amount of tax due will depend on individual circumstances. Future changes in law and tax practice, or in individual circumstances, could affect the amount of tax you may have to pay.

If you're a Scottish Rate taxpayer, the Scottish Rate of Income Tax does not apply to savings income, therefore the tax rates and bands provided in this guide will apply to you as they are the same for all taxpayers across the UK.

Trustees and organisations should take separate advice, as their tax position can be more complex.

Sterling Investment Bond

The investment bond consists of a series of 1,000 separate but identical policies that allow for flexibility when making withdrawals.

The investment bond is:

- a whole of life insurance policy, meaning that it does not have a fixed term or specified end date and provides an element of life cover
- non-qualifying for UK tax purposes, meaning that tax may be due on any withdrawals or surrender (cash-in).

Any gain you make from an investment bond, for example following a withdrawal or surrender, is taxed as savings income (income). No basic rate income tax is due because an equivalent amount of tax is paid on the income and capital gains produced within the fund(s) the bond is invested in and is reflected in the unit price(s). This tax can't be reclaimed.

If you are a basic rate taxpayer, and part of the gain from a withdrawal or surrender takes your income above the higher rate tax threshold in that tax year, you may pay tax on that part of the gain.

If you are already a higher rate (40%) or additional rate (45%) taxpayer, the whole of the gain will be liable to income tax and you will have to pay an extra 20% or 25% income tax respectively subject to any reliefs or allowances you may be entitled to.

If you're a Scottish Rate taxpayer, the Scottish Rate of Income Tax does not apply to savings income, therefore the tax rates and bands provided in this guide will apply to you as they are the same for all taxpayers across the UK.

A chargeable gain may occur whenever there is a chargeable event, as described below.

Chargeable events

Chargeable events that can cause an income tax charge are:

- regular or one-off partial surrenders including any adviser remuneration that is paid that exceed the 5% allowance (described in the 'Withdrawals' section)
- the full surrender of the investment bond (or individual policies)
- the death of the last life insured
- the assignment of the investment bond.

These are all explained in more detail in the sections that follow.

Gains may affect any entitlement you may have to the higher personal allowance (age allowance) and tax credits. Gains may also affect your entitlement to the basic personal allowance if they take your income over £100,000.

If a chargeable event happens, we will send you details of any chargeable gain. We will also inform HMRC where we are required to do so under current tax law.

The examples in this guide do not take into consideration any tax reliefs or allowances available. For more information on tax reliefs and allowances, see page 5.

Types of chargeable event

Withdrawals

Regular withdrawals and adviser remuneration
Under chargeable event rules, each regular withdrawal or adviser remuneration payment is considered to be a partial surrender of the investment bond. As such, for tax purposes, regular withdrawals and adviser remuneration payments are treated in the same way as partial surrenders as explained in the 'One-off withdrawals' section below.

One-off withdrawals
One-off withdrawals can be made in two ways:

Partial surrender

1) By taking a one-off withdrawal equally from all the individual policies that make up the investment bond – this is known as a partial surrender.

   Each year, by which we mean 12 months from the investment bond start date and each subsequent anniversary, you can take regular withdrawals, one-off partial surrenders or make adviser remuneration payments of up to 5% of the amount invested without an immediate tax liability. However, if you take out more than the 5% allowance in any year, this will be classed as a chargeable event and any amount over the 5% allowance, the chargeable gain, may be taxable.

   If you don't use the 5% allowance in one year, you can carry it forward to the next. For example, if £100,000 is invested and you don't take any partial surrenders in the first two years, you can withdraw up to £15,000 in the third year without an immediate tax liability.

If you withdraw your full 5% allowance every year, after 20 years you will have used up all your allowance. So any withdrawals you make after this will be classed as chargeable events and may be taxable, depending on your circumstances.

Taking a large one-off partial surrender, either on its own or when added to regular withdrawals and any adviser remuneration payments, may result in an artificially high tax liability. This is because the tax liability is calculated on the full value of the partial surrender over the 5% allowance, and takes no account of investment performance.

Any tax liability will be calculated in the tax year in which the last day of the investment bond year falls. The investment bond year ends on the day before the next start date anniversary.

Full surrender of one or more whole policies

2) By fully surrendering one or more whole policies that make up the investment bond.

If you fully surrender whole policies, your tax liability will depend on how much the value of each policy has increased, in the same way as a full surrender of the investment bond, as described in the 'Full surrender' section.

Any gain is treated as income for the tax year in which the surrender happens.

Example 1 – withdrawal taken equally from all policies

You pay £100,000 into an investment bond. In the second year its value has increased to £120,000 and you withdraw £40,000. You have not taken any previous withdrawals. The cumulative (total) 5% allowance is £10,000 (£100,000 x 5% x 2). The gain over the 5% allowance is £30,000 (£40,000 – £10,000).

If you are a higher rate taxpayer*, the tax due is £6,000 (20% of the gain for tax year 2018/19).

If you are an additional rate taxpayer, the tax due is £7,500 (25% of the gain for tax year 2018/19).

Example 2 – surrendering whole policies

As there are 1,000 policies, each individual policy is worth £120 in the second year. This represents a gain of £20 for each policy.

You could surrender 334 policies and receive £40,080, resulting in a gain of £6,680 (£20 x 334).

If you are a higher rate taxpayer*, the tax due is £1,336 (20% of the gain for tax year 2018/19).

If you are an additional rate taxpayer, the tax due is £1,670 (25% of the gain for tax year 2018/19).

* and the gain doesn't take your income into the additional rate tax band.

Each policy has its own 5% allowance, so when you surrender a whole policy, any accumulated 5% allowances on that policy are lost. This means the 5% allowance will then be based on the remaining policies. For the example above, in future the 5% allowance will be based on the amount you have invested in the 666 remaining policies.

Important things to consider

We are not permitted to give you tax advice. If you are in any doubt about which method to choose, we recommend that you seek independent advice.

The surrender method you choose may result in significantly different tax liabilities.

Under HMRC rules once a one-off withdrawal has been completed, it cannot be changed or reversed.

Full surrender of the investment bond

When fully surrendering the investment bond, the chargeable event is treated as having happened on the day it is surrendered. Any tax liability is calculated based on the overall gain made on the investment bond.

The overall gain is calculated by adding the surrender value you receive to the value of all previous withdrawals you have taken, then deducting the total value of payments you have made to the investment bond and any previous gains over the 5% allowance.

For example

You invest £100,000 and later surrender it for £120,000. You have previously taken a withdrawal of £10,000 of which £5,000 was taxed as a gain over the 5% allowance.

The tax liability would be calculated as:

£120,000 (surrender value) + £10,000 (previous withdrawal) = £130,000

less £100,000 (original investment) + £5,000 (previous gain over 5% allowance) = £105,000

equals a gain of £25,000 (£130,000 – £105,000).

If you are a higher rate taxpayer*, the tax due is £5,000 (20% of the gain for tax year 2018/19).

If you are an additional rate taxpayer, the tax due is £6,250 (25% of the gain for tax year 2018/19).

* and the gain doesn't take your income into the additional rate tax band.

The surrender method you choose may result in significantly different tax liabilities

Important things to consider

We are not permitted to give you tax advice. If you are in any doubt about any tax liabilities that may arise, we recommend that you seek independent advice.

Under HMRC rules once a full surrender has been completed, it cannot be changed or reversed.

Death

The chargeable event is treated as happening on the day immediately before the death of the last life insured.

The chargeable gain is calculated on the surrender value of the investment bond immediately before death.

On death, if the investment bond is not written in trust, depending on the overall value of the investor's estate, inheritance tax may be due on some or all of the proceeds from the investment bond.

If the investment bond is written in trust, depending on the type of trust, an inheritance tax liability may be reduced. However, most trusts can't be changed so you should seek professional advice before writing your investment bond in trust.

Assignment

Assignment means changing the ownership of an investment bond. Assigning your investment bond to someone else may cause a chargeable event and a possible tax liability.

If an investment bond is assigned in return for money or something of equivalent value, a chargeable event will occur and there may be a tax liability. If it is assigned as a gift then it will not create a chargeable event.

If the ownership of an investment bond is transferred to someone else, we need to be informed by an appropriate 'Notice of assignment'. This protects the legal position of the person to whom it is transferred. Notices of assignment must be given in writing and must state the date and purpose of the assignment.

Tax reliefs and allowances available

Time Apportionment Relief

If you are only resident in the UK for part of the time the plan is in force , and the plan meets certain conditions, it may be possible for gains to be apportioned to allow for this.

If you believe this may apply please contact a tax advisor.

Personal Savings Allowance

If you're a basic rate taxpayer you can receive up to £1,000 in savings income tax-free or £500 if you're a higher rate taxpayer. This is called the Personal Savings Allowance. There is no Personal Savings Allowance for additional rate taxpayers.

Depending on the total amount of savings income you receive from all sources and the level of your Personal Savings Allowance, the amount of your gain that is taxable may be reduced.

Top-slicing relief

Top-slicing relief applies when the addition of the chargeable gain to your taxable income takes you into the higher rate or additional rate tax band. The relief is the amount your tax liability is reduced by, however the example below shows the tax that would be due rather than the amount of relief.

The gain is divided by the number of full years the investment bond has been in force or (for a partial surrender) since the last chargeable event. This produces an average yearly gain, which is treated as the top slice of income in the tax year in which the gain falls. Any tax payable on the top slice is calculated and multiplied by the same number of full years to give the total income tax payable on the gain.

For example

If you are a basic rate taxpayer and have a gain of £14,000 from an investment bond held for seven full years, the top-slice gain will be £14,000 ÷ 7 = £2,000.

The top-slice gain is then added to your taxable income and the tax liability on the total taxable income (including the top-slice gain) is calculated.

Taxable Income	£33,625
Top-Slice Gain	£2,000
Total Taxable Income	£35,625

Basic rate tax is payable on the first £34,500 of taxable income. Higher rate tax is payable on income above £34,500 up to £150,000. Additional rate tax is payable on taxable income above £150,000. These are the limits for 2018/19 tax year.

In this example £1,125 (£35,625 – £34,500) falls into the higher rate tax band. This amount is taxed at 20% and then multiplied by the number of full years that the investment bond has been in force to give the total tax liability on the gain.

£1,125 x 20% = £225

£225 x 7 (years) = a total tax liability of £1,575.

A similar calculation would be required if a chargeable gain takes you from the higher rate tax band to the additional rate tax band.

Corresponding deficiency relief

There is no relief available if you lose money on an investment bond. However, 'corresponding deficiency relief' may be available when an investment bond ends.

The relief will only benefit you if your taxable income (before any gains or top-slice gains are added) is above the basic rate limit (£34,500 in tax year 2018/19). The relief is not available for basic rate taxpayers. The relief does not extend to the additional rate of tax.

Corresponding deficiency relief is available if the chargeable event calculation on death or full surrender shows a negative amount (a loss) and there were gains over the 5% allowance from earlier tax years (because of earlier partial surrenders from the investment bond).

If a loss arises when an investment bond ends, the investor is entitled to a corresponding deduction from their taxable income for that tax year, up to the limit of the previous chargeable gains.

For example

As a higher rate taxpayer you invest £200,000 in May 2009.

In the same tax year you take a one-off partial surrender of £50,000 resulting in a gain over the 5% allowance of £40,000.

Three years later the investment bond is fully surrendered for £170,000.

The gain is calculated as:

(£170,000 + £50,000) – (£200,000 + £40,000) = £–20,000.

The deficiency relief is limited to the lower of the previous chargeable gain (£40,000) or the final loss (£20,000).

The relief is given by extending the basic rate band by the amount of the loss. This means that up to £20,000 of taxable income is chargeable at the basic rate instead of the higher rate that would otherwise have applied.

Sterling Investment Account

Income tax

All income generated by a fund, whether paid as income, reinvested in a fund or accumulated within a fund, may be subject to income tax.

This income must be declared on your normal tax return (whether paid as income, reinvested in a fund or accumulated within a fund). We will send out income tax vouchers each April covering all income generated during the previous year.

Income is either paid (or reinvested or accumulated) as dividend distributions or interest distributions, depending on the type of assets within the fund.

Dividends are taxed as dividend income and interest is taxed as savings income.

If you're a Scottish Rate taxpayer, the Scottish Rate of Income Tax does not apply to dividends or savings income, therefore the tax rates and allowances provided in this guide will apply to you as they are the same for all taxpayers across the UK.

Dividends

The Dividend Allowance* means that you won't have to pay tax on the first £2,000 of your dividend income for the 2018/19 tax year, no matter what non-dividend income you have. The allowance is available to anyone who has dividend income.

You'll pay tax on any dividends you receive over £2,000 at the following rates:

- 7.5% on dividend income within the basic rate band
- 32.5% on dividend income within the higher rate band
- 38.1% on dividend income within the additional rate band

*Please note this allowance has reduced from £5,000 to £2,000 as of 6 April 2018.

Interest

Interest distributions are paid on a gross basis without a tax deduction.

If you're a basic rate taxpayer you'll be able to receive up to £1,000 in savings income tax-free. Higher rate taxpayers will be able to receive up to £500 tax free. This is called the Personal Savings Allowance. There is no Personal Savings Allowance for additional rate taxpayers.

Depending on your personal circumstances you may have further tax to pay. This will depend on the amount of interest and other savings income you receive, and the rate of tax you normally pay.

Income tax – important things to consider

The rate of Income tax you pay and the allowances you receive are determined by your total income including the income you receive within the Personal Savings and Dividend allowances. For more information please contact a tax advisor or visit www.hmrc.go.uk

Capital gains tax

A capital gains tax liability may arise if there is a gain from selling investments in the account.

Investments will be sold in the event of:

- full cash-in
- regular and partial withdrawals
- fund(s) switching
- and to cover the account charges.

If investments are sold for more than their original cost, a capital gain will arise. Tax will be payable when the total gain, taking account of all gains and losses from all relevant investments in the same tax year (and any unused losses from previous tax years), exceeds the current annual exemption (£11,700) for tax year 2018/19.

To see what rate of capital gains tax is payable, the amount of the gain exceeding the annual exemption must be added to your taxable income in the year the investment is sold. For gains falling below the higher rate income tax threshold, the rate for tax year 2018/19 is 10%. Any part of the gain falling above the higher rate income tax threshold is taxed at 20% for tax year 2018/19.

If you're a Scottish Rate taxpayer, the Scottish Rate of Income Tax does not apply to Capital gains tax, therefore the exemption, tax rates and thresholds provided in this guide will apply to you as they are the same for all taxpayers across the UK.

There is no capital gains tax where investments are sold due to the death of the investor.

Other

Fund managers pay stamp duty reserve tax of up to 0.5% when buying or selling investments. Normally, the fund manager takes this tax from the fund and it is reflected in the unit/share price, so it is spread across all investors. However, fund managers may pass on the tax to individuals when they regard a transaction as significant in value.

Depending on the size of an estate on death, inheritance tax may be due on some or all of the proceeds from the account. The account can be irrevocably designated for a beneficiary(s), which would normally be a potentially exempt transfer (PET) for inheritance tax. You should seek professional advice before taking such action.

EU Savings Directive

If a person invests in certain funds and resides in a country outside the UK but covered by the EU Savings Directive, we will need to ask for certain documents to prove their date of birth, address and tax status. We will also have to give HMRC details of income and redemption payments we make. HMRC will pass this information to the tax authorities of the country of residence. We will also disclose information to HMRC where your tax residency means any international Tax Compliance Legislation (such as the Foreign Account Tax Compliance Act (FATCA) or that applying in connection with the Automatic Exchange of Information (AEOI) Agreements requires us to do so.

Sterling Individual Savings Account (ISA)

Income tax and capital gains tax

Currently, you don't have to pay income tax or capital gains tax on any investment gains within an ISA, and there's no need to mention it on your tax return.

Other

Fund managers pay stamp duty reserve tax of up to 0.5% when buying or selling investments. Normally, the fund manager takes this tax from the fund and it is reflected in the unit/share price, so it is spread across all investors. However, fund managers may pass on the tax to individuals when they regard a transaction as significant in value.

As of 6 April 2018, the tax advantages of ISAs have been extended until the point the ISA closes. Previously the tax advantages ceased at the point of the ISA owner's death.

The Additional Permitted Subscription allowance (the amount a surviving spouse or civil partner can pay into their own ISA), will usually be the higher of the value as at the date of the ISA owner's death, or the value as at the date the ISA is closed.

ISAs can't be irrevocably designated for any beneficiary or gifted into trust.

Please let us know if you would like a copy of this in large print or braille, or on audiotape or CD.

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