

Retirement planning for contractors - ISAs

Contractors can make significant tax savings by investing in [Individual Savings Accounts \(ISAs\)](#), especially if they take a long term view with their investments.

According to Tony Harris from [ContractorFinancials](#), ISAs are a very flexible method of saving for retirement: "Contractors can benefit from ISAs in a number of ways. Unlike [pensions](#) they don't attract the same upfront tax boost but are far more flexible in the way contractors can take out their money. ISAs are a highly tax efficient and flexible method of saving for retirement."

ISAs must be funded by a contractor's post tax income so, unlike pensions, they cannot be funded using [limited company](#) income. However, there is no tax payable on the income received from ISA savings and investments.

Contractors can invest up to £10,680 every year in ISAs and the total amount saved can mount rapidly. ISAs are offered by most major financial institutions and contractors can choose which option suits them best, although it is generally best to seek the advice of an independent financial adviser (IFA). In November 2011, the Junior ISA will be introduced with a limit of £3000 pa and will work in the same way as a standard ISA. The child will be able to access the funds when they reach the age of 18.

Which ISA to choose?

There are two main types of ISA contractors can put their money into:

- o Cash ISAs that generally have a variable rate of interest, with instant access and can run almost indefinitely. There are versions that have a higher rate over a fixed term, some may have penalties for early withdrawal and will revert to a variable rate at some stage in the future
- o Equity ISAs, that can perform very well over the long term but have a risk associated because they depend on the performance of the financial markets.

Cash ISAs are like bank or building society deposit accounts, but tend to attract higher rates of interest because the financial institutions view ISA investors as long term savers. Interest is tax free but the cash based return can be low when compared with other options.

The advantage of cash ISAs is that contractors can withdraw their money when they need it, although with some saving schemes this might result in a penalty.

Stocks and shares ISAs

Contractors can choose to invest their money in a managed fund or they can make their own choices about which companies to invest in.

Managed fund ISAs invest in three broad areas:

- o International equity funds
- o Commercial property
- o Corporate and treasury bonds.

The contractor can specify which fund to invest in and can invest via a wrapper that allows funds from many different providers. Their money is actively managed by a professional and it is this manager's expertise that will aim to make money in both good times and bad by selecting relatively good performing shares on the contractor's behalf.

Contractors also have the option of investing in a tracker ISA, which benchmarks the FTSE 100 or some other share index, so the value of the ISA rises and falls accordingly.

Alternatively they can have a self invested ISA, where they personally choose which shares to buy.

"Stocks and shares ISAs are for contractors playing the long game," says Harris, "as the value of the investment can fall below the contractor's initial stake as markets fluctuate."

Flexibility and cost saving

Changes in the rules mean that contractors can opt for investments managed by a number of different fund managers to maximise their investment and still remain within the tax free ISA

“ Stocks and shares ISAs are for contractors playing the long game ”

Tony Harris,
ContractorFinancials

'wrapper'.

Using a range of fund managers within the tax free wrapper can also reduce dealing costs for contractors who opt for stocks and shares ISAs. Contractors can also choose to invest in other financial market items, such as gold, via specialist funds when the market conditions are right.

"If a contractor has the time and the skills, they can play the stock markets themselves within their ISA's tax free wrapper using a fully self invested ISA," continues Harris, "they can net a significant return, although there is also a significant risk that the inexperienced contractor could lose their cash."



Inheritance taxes

As their name suggests, ISAs are held by individuals; you cannot have a joint ISA with a partner in the same way that you can have a joint bank account. Harris says this may need some inheritance tax planning: "Over the course of a contractor's working life, the sums held in ISAs can mount up considerably. As these accounts are held in the name of the contractor, inheritance tax could become an issue."

The major advantage of ISAs is that contractors do not have to pay capital gains tax on the profits from their share dealing/dividends and interest. If a contractor has saved £10,200 over several years and worked the money hard on the financial markets, the profits could be significant, so the tax savings could be considerable.

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Tony Harris is MD of ContractorFinancials, recognised as the specialist independent financial adviser for Contractors.

ContractorFinancials offer jargon free and timely mortgage, pension, insurance and investment solutions tailored to the unique needs of Contractors. [Read Full Profile...](#)

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