Retirement planning for contractors – ISAs/NISAs

Contractors can make significant tax savings by investing in an Individual Savings Accounts (ISAs), especially if they take a long term view with their investments. ISAs are now also known as NISAs, or New Individual Savings Accounts following the reforms introduced in 2014.

According to **Angela James** of **Contractor Wealth**, a financial advisor who specialises in contractor financial advice, 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 £15,000 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 a financial adviser .

Which ISA to choose?

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

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

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.

New rules introduced in 2014 mean that contractors have complete freedom over how much they invest in each type of ISA. They can put all their money in equities, or in cash, or choose to split it between the two

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.

> **"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"**
>
> Angela James, Contractor Wealth

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. By using managed funds within an ISA a client will have access to all manner of assets

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 who invests in a wide range of assets, 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.

Flexibility and cost saving

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 '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 James, "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/NISAs 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. James 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.”

Angela James

Pension Specialist

Contractor Wealth

Angela is a qualified Senior Financial Planner at Contractor Wealth and specialises in pension advice and financial planning for contractors.

Contractor Wealth are a specialist in offering tailored financial solutions for contractors, together with the building of excellent client relationships. **Read Full Profile...**

View all our experts

She adds: “Following the 2014 reforms, on death the ISA can be transferred to the surviving spouse and stay within the ISA wrapper. It is still part of the estate for calculating IHT but it can remain in an ISA. Previously on death, an ISA lost its tax status immediately and the spouse would have to use their own allowances to get the funds back into an ISA.”

Updated: Saturday, January 31, 2015