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Friends Provident International

The advantages of offshore bonds for UK expatriates

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This is an overview of the key benefits available to UK expatriates investing in an offshore bond. It is only a summary and should not be used alone to make any investment recommendation to a client. Friends Provident International Limited (FPIL) does not give tax and/or legal advice.

Capital accumulation – gross roll up

FPIL does not pay tax in the Isle of Man on capital gains and income earned in respect of bond owner investments. Therefore capital gains and income roll up on a gross basis.

Withholding tax may be payable on certain dividend and income payments which cannot be reclaimed. An example is the 30% tax on US share dividends.

No capital gains tax on investment switching

No capital gains tax is payable when switching between different investments inside the bond.

Time apportionment relief

HM Revenue & Customs makes allowance for the fact that some of the profit earned will have arisen whilst the expatriate was not resident for tax in the UK.

The relief can be used by a UK resident who invested in a bond whilst living overseas but has now returned to the UK and wants to surrender.

The chargeable gain will be reduced by the proportionate amount of time spent outside the UK during the life of the bond. The exact number of days is used to calculate the relief.

For example a premium of £100,000 was invested 10 years ago and the bond is being surrendered for a value of £180,000. The investor spent six years in the UAE and four years in the UK.

The chargeable gain is reduced by the fraction $\frac{\mathbf{A}}{\mathbf{B}}$

A is the number of days of non-UK residence

B is the total number of days the bond was in force

$$\frac{2{,}190 \text{ days} \times £80{,}000}{3{,}650 \text{ days}} = £48{,}000$$

Taxable gain = £80,000 – £48,000 = £32,000

On 6 April 2013 new rules for time apportionment relief came into force affecting policies that started on or after this date and also policies that are added to or assigned that started before this date. For a more detailed explanation of the rules please see our time apportionment relief leaflet.

5% tax-deferred allowance

UK resident bond owners can withdraw up to 5% each policy year of the premiums paid for up to 20 years without any immediate liability to income tax.

This allowance is available from the first policy year and any unused allowance is aggregated and can be used to take a withdrawal without an immediate tax liability.

For example if a premium of £100,000 is invested, up to £5,000 is available each policy year for up to 20 years on a tax deferred basis. If no withdrawals have been taken for five policy years £25,000 can be withdrawn in the fifth policy year.

If a withdrawal exceeds the available allowance income tax is payable on the excess amount (see the example below). Once an amount of 100% of the premium has been withdrawn subsequent payments become immediately taxable.

Segment surrender or withdrawal

A segmented bond is issued as a number of individual policies providing an alternative way of taking capital without surrendering the whole bond. One or more segments can be surrendered to raise the required amount and whilst this will be subject to any outstanding surrender charges the chargeable amount to tax will be directly related to the performance of the bond.

For example a premium of £100,000 was invested as 10 segments and after three years is now valued at £115,000. A sum of £34,500 is required.

This differs from a withdrawal whereby cash is taken from across the whole bond. Excess payments above any unused 5% allowance are immediately taxable.

Using the 5% allowance	Using segment surrender
Available allowance =	One segment value £11,500
3 years x 5% = 15% =	£34,500 requires 3 segments
£15,000	Gain on one segment
Excess amount =	£11,500 – £10,000 = £1,500
£34,500 – £15,000 =£19,500	£1,500 x 3 = £4,500
Segment surrender creates a chargeable gain of £4,500 whereas the withdrawal would create a chargeable excess of £19,500.	

An important consideration is that surrendering segments reduces the 5% allowance available as it will be based on the remaining premium attaching to the segments still in existence.

Top slicing relief

Top slicing relief is designed to assist tax payers who would face an increased rate of tax solely due to the chargeable gain being added to their income on surrender. It is available to tax payers in the basic and higher rate bands in the year of assessment.

The gain is sliced by the number of complete policy years the bond was in force, reduced by the number of years of non-UK residency, and one slice is added to the policyholder's income to determine the split between basic and higher rate tax. This relief is not available to trustees.

For example the chargeable gain after time apportionment relief is £80,000 and the bond owner was UK resident for the past seven years having invested in the bond ten years ago whilst living overseas.

The bond owner at the time of surrender is a basic rate tax payer with taxable income after allowances of £28,000.

The gain of £80,000 is divided into seven slices of £11,429 which is added to the taxable income of the bond owner making a total of £39,429 The basic rate tax threshold is £31,785 for UK tax year 2015/2016.

£31,785 – £28,000 = £3,785 x 20% = £757.00

£39,429 – £31,785 = £7,644 x 40% = £3,057.60

Tax on one slice = £3,814.60

Total tax payable on the chargeable gain = £26,702.20

(7 x £3,814.60)

Assignment

It is possible to assign the bond by way of gift from one person to another in order to benefit from the lower tax status in the UK of the assignee. This is often used by spouses and trustees to reduce the amount of tax that would have been payable at their higher rate. Policies gifted by spouses to each other and by trustees to beneficiaries do not create a taxable event.

Estate planning and IHT mitigation using trusts

An offshore bond can be transferred into trust in order to mitigate UK inheritance tax, for succession planning to provide for dependant beneficiaries and to avoid Grant of Probate. We have both discretionary and absolute trusts providing a range of options for estate planning that can be tailored to suit the objectives of the settlor.

Collective and personalised portfolio bonds

Whilst non-UK resident, a bond owner can enjoy the freedom to invest in a wide spread of assets including stocks and shares.

On their return to the UK the bond can be endorsed changing it to a collective investment version whereby it continues to benefit from tax deferred returns.

Failure to endorse the bond results in the bond owner paying income tax on annual cumulating deemed gains of 15% of the premium.

Get in touch

To find out more about the benefits of offshore bonds to UK expat clients, please call us on **+44 1624 821153** or email us at: **alt@fpiom.com**

About Friends Provident International

We are a leading financial services provider, with a reputation for trust, commitment and integrity, offering financial solutions to customers throughout their lives.

Friends Provident International has over 35 years of international experience in offshore savings and investments.

Important Information

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