

Using individual savings accounts to make the most of your savings

Recent years have not been a good time for savers and investors. Interest rates have been at historic lows, the stock market has been volatile and, for many, inflation has outstripped the returns they have received from their savings, eroding the value of their money.

Nevertheless, saving, whether it is for a deposit on a new house, your children's education or your retirement, should still be a key part of your financial plans and there has never been a more important time to make sure your money is working as hard as possible.

Tax-efficient savings

The foundation to your plans should be tax-efficient savings, with any spare cash being put into an individual savings account.

A key benefit of an individual savings account is that you do not pay income or capital gains tax on any growth your money makes, as you might with other savings products. If you earned £500 interest on a standard savings account, even as a basic rate tax payer you would have to pay 20% (or £100) of this to HM Revenue & Customs. Had this money been in an individual savings account, you would have kept the full amount.

There are two types of individual savings account – cash or stocks and shares. Most cash individual savings accounts resemble bank and building society accounts. Stocks and shares individual savings accounts are usually made up of one or more investment funds that spread risk by investing in a range of shares or individual stocks and shares.

Because of the tax advantages of an individual savings account, there is a limit to how much you can invest each year. From 6 April the limit increases from £11 280 to £11 520. The full allowance can be invested

into a stocks and shares individual savings account, or up to half into a cash individual savings account, with the remainder in a stocks and shares individual savings account.

You can either make regular payments into an individual savings account or a lump sum investment. If you opt to make regular payments, they can be flexible, allowing you to stop and start payments, or change the amount to suit your personal circumstances and budget.

Which individual savings account is best for you?

When deciding on the type of individual savings account to invest in, consider what your savings objectives are and how long you want to save for, as well as the risk you want to take with your money.

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For a short-term investment that allows easy access to your money – if you are buying a car or saving for a holiday, for example – then a cash individual savings account could be the best option.

Over the longer term, share-based investments may prove a better option as historically they have provided better returns than cash investments. However, you may feel that investing directly in the stock market is too risky, in which case a stocks and shares individual savings account could offer a middle ground by investing in a range of funds that are professionally managed by experts.

While the stock market has been volatile in recent years, the Barclays Capital Equity Gilt Study 2012 has shown that if shares are held for 10 years, there is a 90% of them outperforming cash, although past performance is not a guide to future performance.

Some providers may sell stocks and shares individual savings accounts that are linked to their with-profits funds. These funds are designed to smooth out the highs

and lows of the stock market, avoiding any volatility with the intention of providing more consistent returns. With-profits products are attractive to those who want to invest in stocks and shares but are concerned about the volatility of the markets.

Shop around

If you already have a cash individual savings account, you are able to change provider if you feel you are not getting the returns you want. Companies often draw customers in with headline rates that are not maintained in subsequent years, so it is worth taking the time to compare accounts and transfer your money if there are better deals available.

If you decide to save into a with-profits individual savings account, one of the main things to consider is the financial strength of a provider. Financial strength means a company can meet its ongoing commitments and it is usually measured by the amount of money it has left over after meeting all of its liabilities. As we have seen with the banking crisis in recent years, a company's size is no indication of financial strength.

Conclusions

Because of the tax-efficient nature of individual savings accounts, they remain a good way to save, no matter what your financial goals may be.

If you have any spare cash and have not yet used up your 2012–13 individual savings account allowance, you have until the end of the financial year on 5 April to invest. When the new tax year starts you will gain a fresh individual savings account allowance, allowing you to continue building up your funds tax-free.

For more information, talk to a financial adviser with understanding of the medical profession who will be able to help you make the most of your savings. **BJHM**

The above information does not constitute financial advice. For further information please speak to your financial adviser.

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