A guide to Investment bonds and care costs

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The cost of care has been increasing and the problem around funding for care will continue to grow over the coming years

Where care is needed, the cost of it will be met by the local authority however the cost of the residential accommodation is means-tested. In England, Scotland and Northern Ireland there are upper and lower limits which can vary by country.

If an individual has assets in excess of the upper limit then they will fund the costs in full, over the lower limit they will have to fund part of the costs, and where assets are below the lower limit there is no requirement to fund.

For those living in Wales there is only an upper limit. Whilst we are only looking at capital assets, it is worth making the point that there are also assessments against income.

Investment bonds

For clarity, the investment bonds we're talking about here are medium to long-term investments that are designed to produce capital growth. Depending on the size of your investment, the returns could also be used to provide a regular income to pay for care fees. They're not to be confused with other investments that have 'bond' in their name, such as guaranteed bonds, offshore bonds or corporate bonds.

When a local authority makes a capital assessment one asset that is listed as being disregarded is the surrender value of any life insurance policy (or annuity). It states: The treatment of investment bonds is currently complex. This is in part because of the differing products that are on offer. As such, local authorities may wish to seek advice from their legal departments.

Where an investment bond includes one or more element of life insurance policies that contain cashing-in rights by way of options for total or partial surrender, then the value of those rights must be disregarded as a capital asset in the financial assessment. So, the guidance does suggest that the local authority seek independent legal advice about the treatment of investment bonds.

It also states that a bond on a life assurance basis should not be included in the capital assessment, meaning that a bond written on a capital redemption basis would be included. A similar position is available in the other countries of the UK. The exclusion is contained in the CRAG guidelines for Scotland and Northern Ireland on how local authorities should assess people for long-term care costs. In Wales the framework has changed as a result of The Social Services and Well-being (Wales) Act 2014 becoming effective from 6 April 2016 and the treatment of investment bonds is consistent with the rest of the UK.

Deprivation of assets

One area to pay attention to is around deliberate deprivation – investing in an investment bond on a life assurance basis, specifically because of care cost concerns. Anyone who places funds into investment bonds, where a motive for the investment is to avoid a care fees charge, runs the risk of triggering the deprivation rules and having the value of those bonds treated as a capital asset for the purposes of means-testing. Trust will only consider questions of deprivation of capital when the resident ceases to possess capital which would otherwise have been taken into account. The timing of the disposal will be agreed when considering the purpose of the disposal. It would be unreasonable to decide that a resident had disposed of an asset in order to reduce his charge for accommodation when the disposal took place at a time when he was fit and healthy and could not have foreseen the need for a move to residential accommodation.

Investment bonds maybe suitable for a number of reasons such as tax efficiency, simplicity, tax deferral, switching of investment funds and so on, however due to the deprivation rules, the favourable treatment of a bond wrapper for assessment is a benefit rather than a reason for using it.

Pros

- Over time, the return on your investment can be higher than with a cash savings account.
- Investment bonds are considered safer than many other investment options.
- If you can hold onto your capital and only use the returns, investment bonds can generate the money needed to pay for care and leave a lump sum to pass on to your children.
- Although money made through investment bonds is taxable, you can normally withdraw up to 5% of the original investment amount each year without any immediate Income Tax liability. This can be drawn monthly to provide a regular income.
- You can avoid putting all your eggs in one basket and potentially reduce the ups and downs of the stock market by investing in a range of funds.
- You can usually switch between funds free of charge, although you might start to be charged if you keep switching funds frequently.

Cons

- You'll normally need to tie up your money for at least five years and might incur big penalties if you cash in your bond early. If you can't tie up the money for this length of time, you might be better off putting your money into an ISA.
- The returns from investment bonds are not always guaranteed. Their value could fall as well as rise and they might not cover the cost of your care.
- Investment bonds are subject to a range of different charges – everything from initial and annual charges to cash-in charges if you withdraw some or all of your money early.
- Although the tax benefits appear attractive at first, investment bonds are probably better described as 'tax deferred' rather than 'tax free'. When you cash them in, the withdrawals are added to any profit made by the bonds and are taxed as income for that tax year.

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