

Ten reasons to do that ISA

By Tom Stevenson, 17 March 2010

The time for procrastination has passed. Here's a checklist for anyone who's still unsure why they should fill in that application form.

Spring has sprung, the evenings are lighter and the garden is demanding your attention again. You can probably think of plenty of reasons not to fill in your ISA application but before the rising sap gets the better of you just remind yourself why the Government's single best tax break is a no-brainer for everyone.



Here are ten reasons why no-one should open an Easter Egg this year until they've used their 2009/10 ISA allowance:

"Personal taxation is heading one way and that is up." Tom Stevenson

- Personal taxation is heading one way and that is up. We're still in the pre-election phoney war but once the new government has got its feet under the table in May (probably), the markets will no longer be prepared to give it the benefit of the doubt. A clear path to fiscal sustainability is a must for whichever party wins the vote and that means lower public spending and higher taxes. The government doesn't give much away on the tax front so what breaks are available should be used to the full. As the tax burden rises, so too does the benefit of avoiding it where you can.
- The ISA tax break is better than it's ever been. Since October anyone over 50 has been able to put £10,200 into an ISA. Those under 50 can do the same from April and, because there's no benefit whatsoever in leaving your ISA until the end of the tax year, this means that some couples can shelter up to £40,800 from the tax-man over the next three weeks or so. For many people the generous ISA allowance means that all their non-pension savings and investments can be tax efficient for ever.
- The ISA break is generous but it is a Use-it-or-lose-it benefit. It's a simple choice. If you choose to invest your money outside an ISA rather than inside you are simply deciding to give a slice of every pound you earn in interest or receive in dividends or make in capital gains to the government. The saving can easily amount to tens of thousands of pounds for regular investors over the years.

- ISAs are fantastically flexible. While I'm a big supporter of pensions, which receive a really attractive up-front tax relief and should be a part of everyone's spread of long-term savings, ISAs have a couple of advantages. First, there are no restrictions on access to ISA funds (this is a disadvantage as well!). Second, you don't even have to declare your ISA holdings to the tax-man.
- There are few restrictions on the investments that you can put into an ISA. You can hold cash or stocks and shares or a mixture of both. The ISA wrapper makes no difference to the risk profile of your investments. It simply means that they can grow and accrue an income tax-free. Really the only question is why you should not put it in an ISA.
- If you are not sure about where the markets are headed, simply park your ISA contribution in cash while you decide. Plenty of people already do that – in fact the Fidelity Cash Park is one of our most popular funds during the ISA season.
- One of the most persistent myths about ISAs is that they are really only any use to higher-rate tax-payers. This is not true. Yes, they are particularly valuable to higher-rate taxpayers (especially for anyone caught by the new 50% rate from April). But basic rate taxpayers can still keep a sizeable proportion of their investment returns that would otherwise have gone to the Government. Remember, too, that younger basic rate taxpayers may become higher rate taxpayers later in life and that an ISA fund that has built up over several years could easily reach a size at which capital gains tax becomes an issue. Once you've protected your savings within an ISA wrapper, you can forget about CGT altogether, which is likely to be an increasing benefit if, as some expect, capital gains is the next target for a tax-hungry government.
- Investing every year in an ISA is a wonderful discipline which forces you to invest in good times and bad and not to fall foul of the very human temptation to invest at the top of the market and to hold back at the bottom. This time last year, most of us would have shied away from investing in the stock market but history has shown that it would have been just the right time to get back into shares. A monthly savings plan is an even better discipline.
- Having risen by around 60% over the past year, the UK stock market is less attractive than it was in March 2009. But, taking a longer view, share prices are still lower

than they were a decade ago. Research shows that this kind of "lost decade" usually leads to much better returns in the next ten years. This is because the most important factor in determining stock market returns is the valuation of shares at the time of purchase. After a lost decade, if the economy has continued to grow, shares are almost by definition at the lower end of the valuation range.

- The fact that taking money out of an ISA means you lose the tax benefit on that investment for good is an excellent incentive to leave your investments alone and to therefore re-invest the income you receive from interest and dividends. The magical power of compounding means that re-invested dividends are the single most important factor in total investment returns over long periods. ISAs encourage you to keep your hands off your money.

Ten good reasons to just say yes to your 2009/10 ISA. What are you waiting for?

Note the value of an investment and the income from it can go down as well as up, so you may get less than you invested. The ideas and conclusions in this column are the author's own and do not necessarily reflect the views of Fidelity's portfolio managers. They are for general interest only and should not be taken as investment advice or as an invitation to purchase or sell any specific security. Past performance is not a guide to what may happen in the future. Investments in small and emerging markets can be more volatile than more established markets. For funds that invest in overseas markets, changes in currency exchange rates may affect the value of your investment.