For financial advisers only

The taxation of onshore bonds

An adviser's guide to understanding chargeable events and top slicing relief

Countrywide Assured

The taxation of onshore bonds: chargeable events

Onshore bonds derive their tax characteristics from their classification as life assurance policies. Countrywide Assured is the life assurance company that owns the underlying investments to which the value of the bond is linked. The company pays tax at a special rate of up to 20% on the income and gains from those underlying investments.

- The bondholder owns the bond, which in most years doesn't produce a taxable income for them such as interest or dividends, as long as they don't exceed the 5% annual allowance (see next bullet point). However, the bondholder may eventually pay income tax – not capital gains tax – on any gains if they take money out of the bond in the form of a 'chargeable event'.

- The bondholder can take up to 5% a year of the original value of the bond when it was set up without incurring an immediate tax liability. However, these 5% withdrawals are added onto any gain when the bond is encashed or matures. These 5% withdrawals are essentially tax-deferred income rather than tax-free income, but this can be helpful if the deferral is to a time when the bondholder pays less tax. The 5% allowance is cumulative; so, if the bondholder doesn't use it in one or more years, they can carry it forward to later years. If adviser fees are taken from the bond, they count towards the 5% allowance.

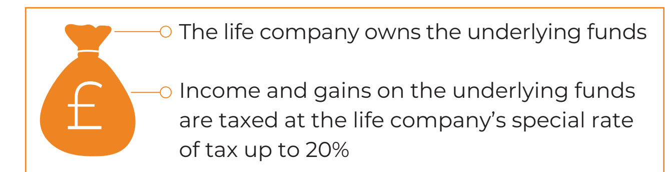
- The chargeable gain on the bond is calculated according to special rules and is treated as the taxpayer's topmost portion of income to determine the rate of tax that applies to the chargeable gain.

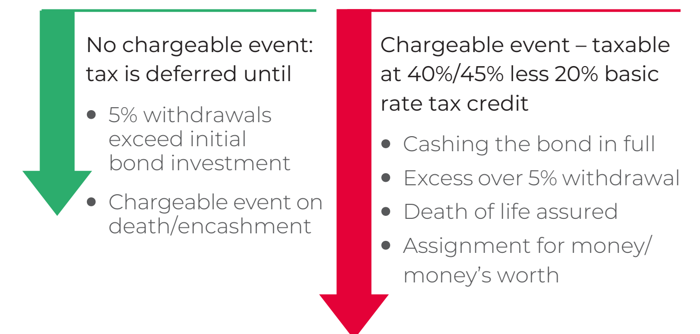
- When the bondholder eventually encashes the bond, they benefit from a 20% basic rate tax credit. This is because Countrywide Assured has already paid up to 20% tax on the underlying investments.
  - So, a basic rate taxpaying bondholder will pay no tax on the gain.
  - A higher rate taxpayer will pay just 20%.
  - An additional rate taxpayer will pay 25% on the gain.
  - However, non-UK taxpayers cannot reclaim the 20% tax credit.

- There is a special tax relief for individual investors called 'top slicing' relief. Top slicing can reduce the effective tax rate for some taxpayers based on the number of complete years the bond has been held since inception.

The taxation of onshore bonds is explained in greater detail below.

The individual or trustee investor owns the bond





The 5% deferred tax allowance for bond surrenders

There is no chargeable event if the bondholder takes no withdrawals whatsoever or withdraws no more than 5% (or one-twentieth) of the initial value of the bond in a tax year. Such withdrawals would normally mean taking 5% from each of the 1,000 identical segments.

- This freedom from tax on 5% withdrawals ceases once the bondholder has taken out the total original value of the investment. That would be after 20 years if the bondholder has taken 5% withdrawals every year. Other patterns of withdrawals could be taken without breaching the 5% rule, such as taking 4% a year for 25 years.
- The 5% withdrawals will be added onto any gain on finally cashing the bond; the 5% withdrawals are therefore essentially tax deferred income rather than tax-free income.
- The 5% allowance is cumulative, so the investor could make no withdrawal in one year and carry forward the unused allowance. For example, the bondholder could take no withdrawals in say the first and second year, but they could then take 15% in the third year.
- Any adviser fee payments made from the onshore bond are treated as withdrawals and are part of the 5% annual allowance. There are (almost always adverse) tax implications if the total of the bondholder's withdrawals and the adviser fees come to more than 5% in a policy year.

Example – the 5% annual deferred tax allowance

An investor who initially invested **£20,000** in a bond could withdraw **£1,000** a year for **20 years** without triggering a chargeable event.

Any withdrawals afterwards would be chargeable events.

Chargeable events – when tax liabilities can arise for bondholders

A bondholder may become liable to pay income tax on their bond when there is a chargeable event. The main triggers are:

- Encashing or surrendering a bond in full.
- Cashing or surrendering one or more of the 1,000 segments of their bond. For example, a bondholder has a bond worth £50,000 and wants to draw £1,000 from it. Encashing 20 of the identical segments would produce the £1,000 she needs.
- Making a withdrawal from all the segments in the bond at rate that exceeds the annual 5% level. For example, a bondholder might decide to cash in 75% of each of all their 1,000 segments that make up their bond – although this would almost certainly be inadvisable because it would create an excess (see the following section on excess withdrawals).
- Death of the life assured leading to a payout under the bond. If there are several people whose lives have been insured under the bond, it's normally set up so that the life company pays out when the last of them has died.
- Assignment of a bond 'for money or money's worth', i.e. by selling it or exchanging the bond in return for a cash payment or something of value.

When a bond is subject to a chargeable event, Countrywide Assured produces a chargeable event certificate (we cover chargeable event certificates in more detail on page 6 of this document).

Excess withdrawals

A withdrawal from across a whole bond that exceeds the cumulative annual 5% allowance is a type of chargeable event called an 'excess event'. Encashing whole segments of a bond is not a partial withdrawal.

- It is generally advisable to avoid excess events, as the name suggests. The excess is taxable as a gain, irrespective of the actual performance of the bond – indeed the bondholder could pay tax on an excess even if the bond has made a loss.
- The taxable amount is assessed in the tax year in which the policy year ends – i.e. the year starting from the anniversary of the bond's inception.
- A bondholder can ask HMRC to adjust the calculation of the gains where they are 'wholly disproportionate' – a term that was defined in recent case law.
- There may be a limited opportunity to recoup tax paid on excesses through deficiency relief. This relief may be available to an individual bond holder as a reduction to their higher rate tax if there's a negative amount on a final chargeable event because of a previous year's excess.

We cover deficiency relief separately on page 14.

The formula for calculating a part surrender is:

The value of the partial surrenders

less

all unused 5% allowances for the current year and each previous year.

The maximum deduction is the amount of initial and subsequent investments/premiums into the bond, which would be reached if the bondholder had taken 5% annual withdrawals for 20 years.

Example – partial withdrawal

Evelyn started the bond on 25 May 2018 with an initial investment of **£10,000** and made no further investments into it. The policy year therefore runs from 25 May to the following 24 May.

She made partial surrenders in the insurance year to 24 May 2024 of **£250** and **£3,450** totalling **£3,700**.

She could have made 5% withdrawals in each of the five years of the bond plus the year of the partial surrender, but she didn't.

5% of the **£10,000** total investment into the bond is **£500** and **5%** of all the previously completed five years is **£500 x 5 = £2,500**. So, the total 5% allowances that she can deduct are **£3,000**.

So, the excess gain is **£3,700** partial surrenders less **£3,000** unused annual **5% withdrawals = £700 gain**.

The **£700 gain arises** on 24 May 2024 in the tax year **2024/25**.

Losses on bonds

If a bondholder makes a loss on a bond when it is finally encashed, there is no tax relief for the bondholder and it is not possible to offset a loss on one bond against a gain on another.

Example – a loss on a bond

If John invested **£50,000** in a bond, took no withdrawals and subsequently encashes it for **£40,000,** he has made a **£10,000** loss on the bond which he cannot use. It would be counted as a £nil gain. If he were to make a gain on another bond of **£20,000** in the same year or later, he would not be able to set the loss against this gain.

A loss on one bond cannot be offset against the gain on another bond, although deficiency relief may apply (see note on deficiency relief on page 14).

Calculating the chargeable gain on an onshore bond

Most chargeable events on onshore bonds arise when the bondholder surrenders the bond or on the death of the life assured. Encashing (surrendering) usually applies to the whole bond or whole segments of the bond.

The basic formula for calculating the chargeable gains (or losses) on encashing (i.e. surrendering) a bond in full is:

Surrender value plus previous partial surrenders (withdrawals)

less

Investment inputs (i.e. premiums paid) plus previous excess gains.

Example – calculating the chargeable gain

The surrender value on Maggie's bond is **£60,000** and she has taken eight years of 5% withdrawals at **£3,000** a year (i.e. £24,000). So, her total proceeds from the bond amount to **£84,000**, because her **£24,000** cumulative 5% withdrawals are added back to the **£60,000** surrender value to calculate the chargeable gain.

Her original investment input was **£60,000** and she has had no excess gains. So, Maggie's chargeable gain in this case is **£84,000 less £60,000 = £24,000**.

Maggie has also realised a loss on another bond, but she cannot offset this loss against her chargeable gain on this bond.

Death benefit value

When the bond closes on the death of the life assured – the payout will be slightly higher than the surrender value, because there is a small death benefit of an extra 0.1% of the surrender value.

- The chargeable gain or loss is based on the surrender value at the date of death plus previous withdrawals – not the actual payout (including the small amount of life cover) plus withdrawals..
- Where the policy has made a gain, the chargeable event certificate that Countrywide Assured provides to bondholders will specify the chargeable gain.

Chargeable event certificate

Countrywide Assured will tell the bondholder that they have made a gain on their bond and how much it is in a chargeable event certificate. It will set out:

- The type of event – e.g. full surrender or excess.
- Date of the event – important for deciding which tax year the income falls.
- Number of years since inception of the bond or since last the last chargeable event – this determines the possible amount of top slicing relief available (we cover top slicing relief in more detail on page 8).
- The amount of gain rounded down – e.g. the total amount of gain on which tax may be payable.
- Income tax that is treated as paid – which essentially confirms that the bond is an onshore or UK policy.
- Amount of tax treated as paid (which is rounded up). This is the tax credit for basic rate tax deemed to have been paid on the onshore bond gain, i.e. normally 20% of the amount of the gain.

Tax rate payable by the bondholder on an onshore bond chargeable gain

The chargeable gain is taxed at the rate of income tax that would apply if the gain is added to the bondholder's other income. There are some special rules that apply to bonds:

- Onshore bondholders don't pay basic rate tax on a chargeable gain, because they benefit from a 20% income tax credit. But they could have to pay income tax to the extent that they are liable to higher rate tax or additional rate tax on the chargeable gains. The higher rate tax on a chargeable gain is 20%, and the additional rate tax is 25%.
- Bondholders who have been non-UK resident for a time may benefit from a relief called 'time apportionment reduction' (we cover this on page 11).
- There is a special relief called 'top slicing' based on the number of years the bond has been held. This is explained in detail on page 8.

Example – tax payable on a chargeable gain: the basic rate tax credit

An additional rate taxpayer as a chargeable gain of **£10,000** on which the **45% rate of tax applies**. The tax would be **£10,000 x (45% - 20%) = £2,500**.

If this person happened to be a **higher rate (40%) taxpayer**, the tax would be **£10,000 x (40% - 20%) = £2,000**.

If they were a **basic rate taxpayer (20%)**, the tax would be **£10,000 x (20% - 20%) = £0**

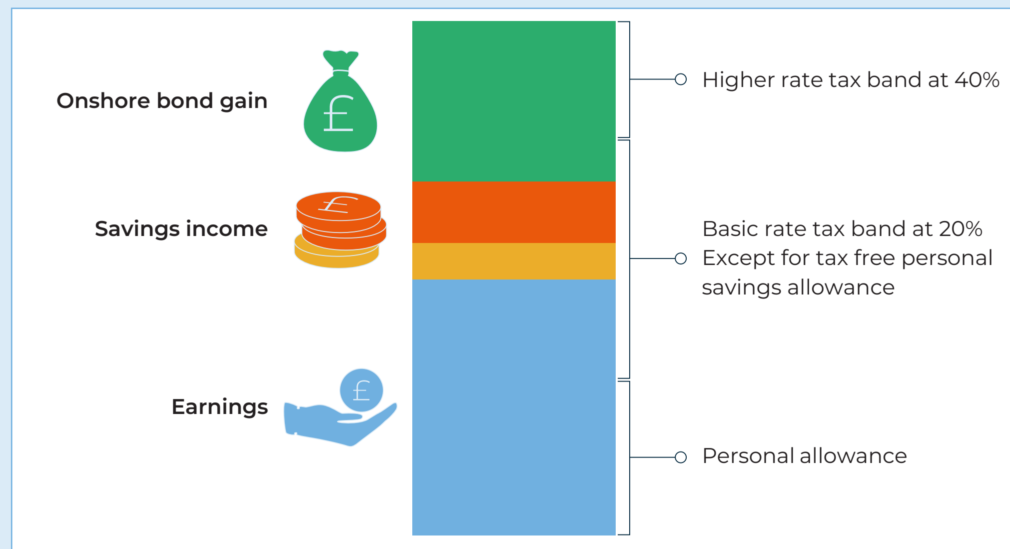
Onshore bond chargeable gains in the priority order for taxing income

Onshore bond chargeable gains are taxed at the investor's top marginal rate or rates of tax, even though they also count as savings income for the purposes of the savings allowance and starting rate. In the fixed priority order for calculating income tax, onshore bond gains come last:

- First, earnings (like salary and pensions)
- Then savings income (like interest)
- Then dividend income
- Finally, onshore bond gains.

(Capital gains come after that.)

Example – the priority order for charging income tax on an onshore bond chargeable gain



In the diagram above, Ellen, the bondholder, has earnings that straddle the personal allowance of **£12,570** and the basic rate band of up to **£50,270** in the tax year 2024/25.

Ellen is resident in England. Scotland has slightly different tax rates.

The basic rate band in this instance also covers their savings income – apart from the tax-free savings allowance (**£1,000 for basic rate taxpayers and £500 for higher rate taxpayers**). It also covers part of the chargeable gain on the onshore bond.

In Ellen's case, part of the chargeable gain on the onshore bond falls into the higher rate tax band. An onshore bond chargeable gain can shift a person who just pays basic rate tax on their income up to being a higher rate taxpayer on some or all their onshore bond chargeable gain. Or it can take someone with a 40% marginal rate of tax into the 45% additional rate band.

The taxation of onshore bonds: top slicing relief and the tax calculation

Top slicing is a valuable relief that can reduce the tax liability on onshore bond chargeable gains for some individual investors. The relief is essentially based on the number of complete years an investor has held a bond since inception.

- Top slicing relief can affect the rate of tax that applies to the onshore bond chargeable gain where the gain would otherwise take the taxpayer into a higher tax bracket.
- Top slicing relief is not available to trustees, personal representatives or companies.
- If there has been an excess withdrawal – i.e. a withdrawal that exceeds the 5% provision – the top slicing relief is counted from the date of the excess. So, the relief can be nil or very low where the investor has incurred an excess in the recent past.

Top slicing relief allows a bondholder to set the chargeable gain in the calculation against their available personal savings allowance and any basic rate tax band for every full year the onshore bond has been held, rather than for just one year.

Depending on the circumstances, top slicing relief can make a big difference to the amount of tax payable on the gain or possibly it may make no difference at all in some cases.

The broad effect of top slicing relief is to divide the onshore bond chargeable gain by the number of years the bond has been held. This determines how much of the chargeable gain should be added to their existing income to calculate the tax rate that should apply to the gain.

The main steps for calculating top slicing relief

The main steps for calculating top slicing relief on an onshore bond chargeable gain are as follows:

1. **Calculate the bondholder's total taxable income for the tax year, including the onshore bond chargeable gain, and identify how much of the chargeable gain falls within the relevant tax bands.** These income tax bands could be the starting rate for savings, personal savings allowance nil rate, and basic, higher or additional rate bands as appropriate. The chargeable event certificate shows the amount of the chargeable gain. In the top slicing relief example calculation on the next page, Amanda's chargeable gain straddles both the basic and higher rate bands.
2. **Calculate the total tax due on the chargeable gain for the tax year across all the relevant tax bands.** Deduct basic rate tax treated as paid to find the total liability for the tax year. At current rates of income tax, this is 20% of the chargeable gain and is shown on the chargeable event certificate.
3. **Calculate the annual equivalent of the chargeable gain based on the years held.** The annual equivalent is calculated by dividing the chargeable gain by the number of complete years (12-month periods) since date of inception or the date of the last excess event (if there has been one). The chargeable event certificate shows the number of complete years from inception that the bond has been held. This number is used to calculate the top slicing relief.
4. **Calculate the bondholder's tax liability after top slicing relief.** Deduct basic rate tax treated as paid on the annual equivalent and multiply the result by number of years for top slicing relief. This gives the total income tax liability on the onshore bond chargeable gain after top slicing relief.

Example 1 – top slicing relief calculation

Amanda has an onshore bond chargeable gain of **£50,000** in **2024/25** when she made a full surrender of an onshore bond that she has held for five complete years. Her employment income for the tax year **2024/25** is **£45,000.**

Amanda is given a basic rate tax credit on the chargeable gain. This means she is treated as if she had paid **20% tax** on the full amount of the gain, **i.e. £10,000 (20% of £50,000).**

- Her personal savings allowance nil rate tax band is **£500** because she is a higher-rate tax payer for 2024/25. The higher rate tax band starts at £37,700 after taking account of the personal allowance (i.e. £50,270 less £12,270).
- Amanda is not eligible for the starting rate for savings income because her non-savings income is above £17,570 – the personal allowance plus £5,000.

Step 1 – Calculate total taxable income for the tax year, including the onshore bond chargeable gain, and identify how much of the chargeable gain falls within the relevant tax bands.

Amanda's total taxable income is **£95,000**, which falls within the various tax bands as follows:

Source	Amount £	Band	Rate	Tax Due £
Employment	12,570	Personal allowance	-	0
Employment (Total £45,000)	32,430	Basic rate	20%	6,486
Chargeable gain	500	Personal savings allowance	0%	0
Chargeable gain	4,770	Basic rate	20%	954
Chargeable gain (Total £50,000)	44,730	Higher rate	40%	17,892
Total liability on chargeable gain	(954+17,892)	-	-	18,846

Step 2 – Calculate the total tax due on the chargeable gain for the tax year across all the relevant tax bands.

Total tax chargeable on the gain	**£18,846**
Less basic rate tax treated as paid	**£10,000**
Total liability for the year	**£8,846**

Step 3 – Calculate the annual equivalent of the chargeable gain based on the years held

The annual equivalent is the total gain divided by the number of years the policy has been in force. In this case the annual equivalent is **£50,000/5 = £10,000.**

Step 4 – Calculate the tax liability on the chargeable gain after top slicing relief

The liability to tax on the annual equivalent is as follows:

Source	Amount £	Band	Rate	Tax Due £
Employment	12,570	Personal allowance	-	0
Employment (Total £45,000)	32,430	Basic rate	20%	6,486
Chargeable gain	500	Personal savings allowance	0%	0
Chargeable gain	4,770	Basic rate	20%	954
Chargeable gain (Total £10,000)	4,730	Higher rate	40%	1,892
Total liability on chargeable gain	(954+1,892)	-	-	2,846

- The basic rate tax treated as paid on the annual equivalent is £10,000 x 20% = £2,000.
- The higher rate tax liability for the one-fifth slice of £10,000 is £2,846 - £2,000 = £846.
- Then multiply by the number of years the bond has been held (5) to find the total income tax liability after top slicing relief: £846 x 5 = £4,230,
- The effective higher rate of £4,230/£50,000 = 8.46%
- If there had been no top slicing relief, the tax liability would have been £8,846/£50,000 = 17.69%.
- The top slicing relief in this case is therefore worth £4,616 (i.e. £8,846 less £4,230).

Example 2 – top slicing relief calculation

In some cases, top slicing relief can reduce to nil the higher or additional rate tax on an onshore bond chargeable gain.

If Amanda had held the bond for ten years rather than just five years, the **£50,000** chargeable gain would have been divided by ten and the slice added to her income in step 3 would have been only **£5,000**, which would not have been enough to bring the chargeable gain into a higher rate tax charge.

Overseas residence relief – the time apportionment relief

Time Apportionment Relief (TAR) can reduce the taxable gain on bonds. There is generally no UK tax to pay in a tax year in which the bond holder is not resident in the UK. The relief is based on any periods when the bond holder owned the bond was not a UK resident but a chargeable event occurs after they have returned to UK.

How TAR works

A UK resident bond holder can claim a reduction in a chargeable gain on a bond if they have been not resident in UK for part of the investment period. The TAR reduces the amount of gain that is subject to tax – not necessarily the amount of tax itself.

The reduction in the gain is based upon the number of whole days of non-residence over the relevant period equal to:

Chargeable gain x (number of days of non-UK residence) / (total number of days in the period)

Example

Rod had almost exactly six years (**2,200 days**) of non-UK residence during the 10-year period (**3,700 days**) in which he owned his onshore bond. The chargeable gain for the whole period is **£60,000** and occurred after he had taken up UK residence again. So, the reduction in the gain is:

Chargeable gain of **£60,000 x 2,200 days** of non-UK residence / **3,700 total days** in the ownership period

= £35,675.67, bringing down the chargeable gain to **£24,324.33**.

Conditions for qualifying for TAR

- The individual's non-UK residence must not have been temporary, which among other things means that they must have been not resident in UK for at least five years. Tax residence is determined by a statutory residence test and it is highly advisable to document fully all periods of non-UK residence.
- Onshore bonds that were started before 6 April 2013 do not generally qualify for the relief. There are exceptions to this rule where on or after 6 April 2013,
  - either the policy was varied and this increased the benefits
  - or there was an assignment of the rights in the policy to the individual now claiming the relief.
- The relief applies to the individual who is liable to income tax on the gains and only relates to their periods of non-residence – not those of any previous owners of the bond.
- But if a bond holder assigns a bond to their spouse or civil partner with whom they live, the investment period can include any periods of non-UK residence of the transferring spouse or partner.
- Trustees may also be able to claim TAR in some circumstances. They must be liable to tax on the gain because there is a deceased settlor who died in an earlier tax year and who was UK resident at the date of their death. The period of non-residence for which the trustees can claim is based on the settlor's residence history.
- Legal personal representatives of a deceased person may be able to claim TAR if the chargeable event gain occurs during the estate administration period. The period of non-residence for which they can claim is based on the deceased person's residence history.
- Where a policyholder has claimed TAR, it may reduce the number of years for the top-slicing calculation.

The personal portfolio bond rules

Onshore bonds are subject to the Personal Portfolio Bond (PPB) rules restricting the links that can be made to the value of such underlying investments as private company shares or real property that has been transferred to the insurance company. Offshore bonds are also subject to these rules.

The PPB rules apply to assets that are much more personal to the bond holder than the normal type of investments. The PPB rules are aimed at preventing tax avoidance on these assets by postponing gains until the bond is encashed.

Wealth managers who are running portfolios for clients within the tax wrapper of a bond need to be aware of the rules and how they could affect the way in which they run portfolios for clients.

Scope

The PPB rules apply where the bond value is linked to an index or property that the bond holder (or someone connected to them) can select.

- HMRC provides a list of assets and indices that fall outside the PPB rules. They include the insurance company's own internal funds, units in an authorised unit trust, shares in an OEIC or investment trust and cash.

- Even if an investment is on the exempt list, the insurance company must make the opportunity to invest in it available and marketed to a class of potential investors to prevent the bond being treated as a PPB. What makes a bond a PPB is the scope of the bondholder's ability to choose the investment rather than what they actually choose.

The charge

The PPB regime levies a penal annual income tax charge on the bond holder. The tax charge is based on a special PPB excess, even though the bond holder may not have withdrawn any payments from the bond.

The excess is calculated every year and is 15% of the following amount:

The initial investment (premium) into the bond

less

cumulative withdrawals

plus

subsequent excesses

- The resulting excesses are highly likely to exceed the economic gain on the bond, although they may well be offset by deficiency relief (see page 14).

- Top-slicing relief is not available on PPBs, although the basic rate tax credit does apply to onshore bonds.

The charge is made on the last day of the bond's insurance or policy year, which starts on the day bond was taken out and ends on the day before the anniversary of the start day.

Example

1

In the first year, the excess is 15% of the initial investment into the onshore bond, less any withdrawals. The bondholder has a potential higher or additional rate tax liability.

So, if the initial input into the bond was £100,000 and the bondholder took no withdrawals, the excess would be £15,000, on which a higher rate taxpayer would be liable for £3,000 tax.

2

In the second year, the excess is 15% x (the initial investment plus the previous excess less total withdrawals).

So, with the £100,000 bond and assuming no further withdrawals, the excess would be 15% x (£100,000 + £15,000) = £17,250, on which the higher rate charge would be £3,450.

3

In the third year, the excess is calculated on the same basis. On the same assumptions the excess and the tax charge would be even higher than in the first or second years and would be higher still in later years.

So, with the £100,000 bond and assuming no further withdrawals, the excess would be 15% x (£100,000 + £15,000 + £17,250) = £19,837, on which the higher rate charge would be £3,967.

4

In the final year when the bond is encashed, there's no excess charge but the encashment or maturity is likely to have generated a very high tax charge in relation to the actual economic profit on the bond, with no tax relief for the resulting deficiency.

So, if the above bond had been cashed in the fourth year and the proceeds were £120,000, the total PPB gains would be £15,000 + £17,250 + £19,837 = £52,087. The total tax on this amount for a higher rate taxpayer would be £3,000 + £3,450 + £3,967 = £10,417 and it is likely to have suffered a similar amount of tax within the fund. In contrast, the economic gain on the bond would be £120,000 - £100,000 = £20,000.

Losses on onshore bonds and deficiency relief

Losses on onshore and offshore bonds

If an investor makes an investment loss on a bond when it matures or finally encashed, there is no tax relief for the loss for the investor and it is not possible to offset a loss on one bond against a gain on another. The only very limited relief for certain losses is deficiency relief.

Example

John invested **£50,000** in a bond, took no withdrawals and subsequently encashed it for **£40,000**. He has therefore made a **£10,000** loss on the bond that he cannot use against the profit on another bond or any other investment. It would be counted as a **£nil** gain for the year. So, if John were to make a gain on a bond of **£20,000** in the same year or later, he would not be able to set the loss against the gain.

Deficiency relief

Deficiency relief may be available to an individual bond holder as a reduction to their higher rate tax, if they have a negative amount on a final chargeable event because of a previous year's excess.

The conditions for the relief are:

- A calculation of a gain for a surrender, maturity or death shows a negative figure or 'deficiency'. This happens where total deductions plus previous gains exceed the total benefits.
- The person who is chargeable on the gain is an individual. It is not available to trustees, legal personal representatives, executors or companies.
- The bond holder claiming the relief must have made earlier surrenders or part assignments of the bond.

Deficiency relief is given as a reduction in the bond holder's higher rate tax liability for the bond's final year when the bond comes to an end.

- There can be no tax reduction unless the bond holder has some income that is liable to income tax at the higher rate or dividend upper rate. Deficiency relief provides no benefit to a basic rate taxpayer.
- The relief does not reduce the income tax on income liable at the additional rate or the dividend additional rate.
- Where the bond holder has no dividend income, the deficiency relief is given by extending their basic rate tax band by the amount of deficiency relief.
- If the individual has dividend income, the calculation is more complicated. But the effect is that the deficiency relief on that income is limited to 25% in 2024/25, i.e. the difference between the upper rate (33.75%) and the ordinary or basic rate (8.75%) on dividends.

Example – relief not limited by the amount of the earlier excess

Rachel took out a bond on **5 October 2020** with an initial investment of **£20,000.**

On 27 September 2022 she withdrew £8,000 from the policy by a part surrender i.e. an excess event. The gain is £8,000 less £2,000 (5% annual allowances for two years) = £6,000.

On 14 November 2024 she surrendered the policy for £13,000. She was UK resident throughout.

Her only taxable income (after personal allowances) in 2024/25 is employment income of which £3,000 is taxed at the higher rate of 40%.

Tax treatment
The first 'insurance year' for the bond runs from 5 October 2020 to 4 October 2021; the second insurance year runs from 5 October 2021 to 4 October 2022, and so on, until the final insurance year, which runs from 5 October 2023 to 14 November 2024.

Year 2: The 'periodic calculation' for 4 October 2022 shows an excess of £6,000 (that is, £8,000 less £20,000 x 2/20). So, the part surrender of £8,000 created an 'excess event' on 4 October 2022 and a gain of £6,000, which formed part of Rachel's taxable income for 2022/23.

Final year: The gain calculation on the surrender is: total benefits less total deductions less previous gains.

- Total benefits are £8,000 + £13,000 = £21,000.
- Total deductions are the initial investment into the bond of £20,000
- Previous gains come to £6,000, which is the gain on the earlier 'excess event'.

The gain calculation
is £21,000 less £20,000 less £6,000 = minus £5,000. The amount of deficiency is £5,000, which is less than the amount of the earlier excess gains.

The amount of deficiency available for relief is therefore £5,000 (the amount of the overall deficiency) which is available against Rachel's total taxable income in tax year 2024/25, as follows.

Rachel's taxable income falling in the higher rate tax band is £3,000, which is relieved by deficiency relief of £3,000. Effectively, the basic rate band is extended by £3,000 so that an additional £3,000 of Rachel's employment is taxed at basic rate rather than higher rate.

The balance of the deficiency relief is £2,000 which she loses. She cannot:

- Use the relief in 2024/25, or
- Carry the relief forward to future years, or
- Carry the relief back to previous tax years.

Relief limited by the amount of the earlier excess

If Rachel had surrendered the bond in 2024/25 for £10,000 rather than £13,000.

Tax treatment
Year 2: As before, there is an 'excess event' on 4 October 2022 and a gain of £6,000.

Final year: the total benefit is now £8,000 + £10,000 = £18,000. Total deductions (£20,000) and previous gains (£6,000) are as before.

The gain calculation is £18,000 minus (£20,000 plus £6,000) = minus £8,000. Because the initial investment was higher than the total benefits, the amount of deficiency available for relief is limited to the amount of the earlier chargeable event gain; that is £6,000.

Any questions?

If you have any questions please call us on 0333 0155600

Or go to **countrywideassured.co.uk**

Financial advice

This note provides details of the structure, taxation and uses in financial planning of onshore life assurance bonds and is for your guidance only. Countrywide Assured plc (“Countrywide Assured”) accepts no liability for any action taken or not taken by an individual or firm as a result of the contents of this material.

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