Association of International Life Offices
AILO

An investment product designed for **everyone...**

A guide to offshore bonds

This guide explains some important generic facts about offshore bonds and is designed to complement the specific advice and information provided to you by your financial adviser.

The guide is published by the Association of International Life Offices, an independent body whose member companies have more than £25 billion of client funds under management held within offshore bonds.

Advice and **recommendations**

Financial advisers recommend offshore bonds to their clients as part of the provision of 'best advice'. Your financial adviser will work with you to establish your financial goals, undertake an analysis of your needs and assess your attitude to investment risk. Under rules governed by the Financial Services Authority, your adviser will then consider the suitability of a range of financial solutions from the whole market and will recommend an offshore bond when this is the most suitable solution for you.

Offshore **Myths...**

Offshore is..."Only for the very wealthy"

Many thousands of UK people invest offshore every year and most would not consider themselves to be very wealthy. Offshore bonds are commonly used in planning to mitigate inheritance tax, capital gains tax and income tax. Offshore investments can start from as little as £10,000.

Offshore is..."Based in 'questionable' tax havens"

The offshore companies that are members of AILO operate from some of the world's most highly regulated jurisdictions. Republic of Ireland and Luxembourg, like the UK, are full EU Member States, and the Isle of Man and Channel Islands are UK dependent territories. These jurisdictions have been thoroughly scrutinised by global monitoring bodies and have received recognition for their strong regulatory controls and investor protection measures.

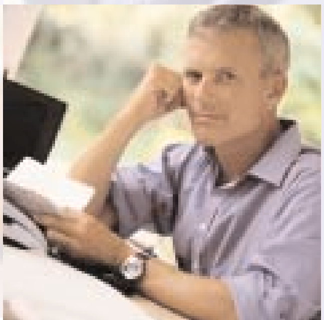
Financial **planning**

There are a number of client scenarios that are most likely to result in your financial adviser recommending an offshore bond to you.

Perhaps the most common situations are where:

- the offshore bond forms part of your wider inheritance tax planning
- you plan to become (or are already) an expatriate e.g. working or retiring outside of the UK
- you wish to defer cashing-in your investment, or taking income from it, into a period when you will be within a lower income tax band
- you require access to types of funds which are not commonly available within the UK domestic insurance bond market

Offshore bonds are also frequently used by financial advisers to provide their clients with a wider choice of options as they seek better medium to long term returns than cash deposits through exposure to equities and alternative investments.



Offshore bond **benefits**

The specific benefits of an offshore bond depend upon your individual circumstances.

However, there are a number of generic benefits for UK residents which tend to apply in most situations:

- **Virtual tax-free growth**
  Often referred to as the 'gross roll-up' effect, investment in an offshore bond grows virtually free of year-on-year income tax and capital gains tax charges, unlike comparable onshore bonds which suffer tax on any growth. Small amounts of irrecoverable withholding tax may be payable on certain investment funds.

- **No capital gains tax**
  Fund switches made within offshore bonds do not trigger a capital gains tax liability. Such switches within a portfolio of onshore direct equity or unit trust investments would incur a capital gains tax charge in the tax year during which the switches were made. Offshore bonds often therefore provide a more tax efficient structure for active investment management.

- **Access to your money**
  Most offshore bonds enable you to have access to some or all of your investment monies should you need to. As offshore bonds are long term investments there may be some penalties which apply if you withdraw your money in the early years.

Offshore **Myths...**

Offshore products..."Are unregulated"

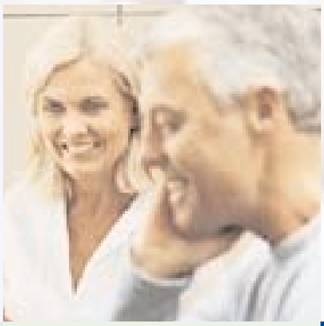
Offshore bonds are provided by reputable life companies, most of whose brands are household names in the UK. These companies are fully covered by their home state regulation. Products sold in the UK also have to meet all the Financial Services Authority's product and promotion rules.

Offshore products..."Are complicated and expensive"

Offshore products are no more complicated than equivalent products in the UK domestic market, with companies making their products simpler and more transparent in line with UK consumer demands. Offshore products can be slightly more expensive than their domestic equivalents, but this marginal difference can be more than offset by the tax advantages that can be obtained.

Offshore is..."All about tax evasion"

Offshore bonds are recommended by financial advisers within their regulated advice process as Inland Revenue compliance-based tax planning solutions. The use of offshore bonds should not be confused with 'aggressive' or complex tax avoidance schemes. Offshore bond customers are ordinary law abiding citizens, not tax evaders!



You can take regular withdrawals from most offshore bonds, accessing your capital in a tax efficient way by withdrawing up to 5% of each investment amount every year as "income". This 5% amount can be taken every year for 20 years, or accumulated over a number of years and withdrawn less frequently without triggering a 'chargeable event' for tax purposes (a 'chargeable event' occurs when you withdraw in excess of 5% a year, or you cash-in your bond in full, triggering an income tax charge).

Tax control

Tax deferment is a key feature of offshore bonds. This enables you to choose when a tax charge may occur, as this will be when you cash-in some or all of your bond. The tax payable at the point of a chargeable event will depend on your highest marginal rate at that time. This allows you to defer such an event until you are either no longer a tax payer or have moved from being a higher rate tax payer to a lower or basic rate tax payer or have moved to a country with lower taxes.

Inheritance tax planning

Structuring your assets through an offshore bond held in Trust can mitigate, or avoid altogether, taxes due when transferring wealth. Assets above the nil rate band (the threshold above which inheritance tax applies) which are not held in Trust may be liable to inheritance tax at 40%. Additionally, an offshore bond and Trust can be structured to allow access to the funds prior to your death.

Self assessment friendly

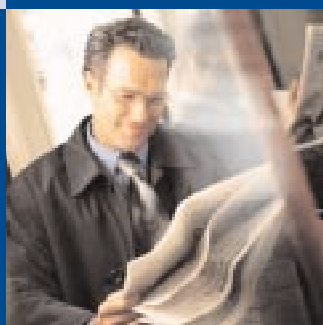
As offshore bonds are 'non-income producing assets' there is nothing for you to report to the Inland Revenue until a chargeable event occurs e.g. when you cash-in more than 5% of each amount invested. You do not have to include any information on your tax return before this point, compared with the potentially complicated requirements for reporting a portfolio of unit trusts. At the point that you do need to include information on your tax return under self assessment, it is also generally much simpler to report income from an offshore bond.

Non-UK status

As offshore bonds are not UK-based investments, this can help you mitigate your UK tax bill if you are a UK expatriate or a foreign national living in the UK.

A fundamental benefit of an offshore bond is that it provides a 'tax wrapper' around your investment choices, with potentially more favourable tax treatment than an onshore equivalent.

Please remember that benefits are not guaranteed and that the value of investments may go down as well as up.



Investment **Choice**

Offshore bonds often feature a strong range of the company's own individual offshore funds and managed offshore funds specifically tailored to fit investors' attitudes to risk.

Offshore bonds also offer access to all the household name fund managers in the UK market, plus many more international and specialist fund managers. This allows you to access a wider range of asset classes when your financial adviser is reviewing your all important asset allocation.

The investment choices within offshore bonds cover all the major world regions and sectors, and the full risk spectrum from low risk capital guaranteed funds through to hedge funds and higher risk specialist funds.

Global companies

The companies which offer offshore bonds are mostly subsidiaries of major UK, European or US financial services companies which are based in the main offshore jurisdictions. The parent companies, with their significant financial strength, stand behind their smaller, more specialist offshore subsidiaries.

These companies operate to the same high standards as UK domestic companies. In addition, over the last 20 years or more, these companies have developed particular expertise in dealing with UK and international clients' offshore investments.

Offshore **Myth...**

Offshore investment is..."exotic and risky"

Offshore bonds provide access to all the UK household name fund managers and funds, with a full range of risk profiles, from capital guaranteed funds through to higher risk specialist funds. They also give wider access to international funds and asset classes from global investment firms which are not available 'onshore'.

First class jurisdictions

Most UK clients set up their offshore bond with companies based in the UK dependent territories, such as the Isle of Man and Channel Islands, or EU Member States such as Republic of Ireland and Luxembourg. All these jurisdictions benefit from stable governments, strong regulatory controls and investor protection measures.

A number of independent reviews in recent years by global monitoring bodies have confirmed that these jurisdictions benefit from strong reputations and a specialist offshore financial services support infrastructure.

To maintain this position, these jurisdictions continue to adopt proactive anti-money laundering procedures. In today's society, the vigilance against terrorist or drug money laundering does mean that the procedures for vetting all offshore investors need to be thorough. You will need to provide confirmation of your own identity and also the source of your funds.

Summary

You can be confident that your financial adviser's recommendation to invest via an offshore bond will provide you with a flexible and tax-efficient 'wrapper' for your investments.

This is an

Association of International Life Offices publication

The Association of International Life Offices was formed in 1987 by a number of companies supplying insurance and investment services in many areas of the world. The Association encourages the integrity and professionalism of its member companies while representing their interests with governments and regulators.

The Association's membership comprises over thirty companies, from seven jurisdictions, with parent companies originating in fourteen different countries and is listed opposite

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