Investment Bonds

Investment bonds are investment products usually offered by life insurance companies. Income earned within the bond is retained in the bond until it is redeemed. Although investment bonds can generally be redeemed at any time, they are usually best regarded as medium- to long-term investments because withdrawals after 10 years can be tax free in the hands of the bond holder.

Income on Investment bonds is subject to income tax in the hands of the product provider. In the case of insurance companies, the gross tax rate is 30%. If the bond is held for more than 10 years, the income earned on it becomes tax free when redeemed.

If the bond is redeemed within 8 years, the income on the bond is assessable in the hands of the bond holder at their marginal rate but the bond holder is entitled to a tax rebate for the tax already paid by the provider.

If redeemed during Year 8, two-thirds of the bonds will be subject to a tax credit and subsequently taxed at the client's marginal rate. If redeemed during Year 9, one-third will be subject to this arrangement. The rest of the funds will be tax free.

Investment bonds are classed as assets for the Centrelink/DVA Assets Test, and are deemed as Financial Investments for the Incomes Test.

Bonds can be purchased by people on their own behalf or jointly with another person. Companies are also eligible to purchase them and there are ways to establish bonds for the benefit of children.

The benefits of Investment bonds may include: -

- Very simple - the bonds require no management by the investor.
- Bonds may be cashed in either in part or whole at any time.
- Additional investments to the original bond - up to 125% of the previous year's contribution can be added without affecting the tax status of the total sum invested. Thus, it is possible that money invested in the 9th year qualifies for the tax concession.
- No capital gains tax applies.
- No tax is payable when the bond is redeemed in the instance of accident, illness or serious financial difficulties of the life insured, the death of the life insured or after the expiration of 10 years from the date of the original investment.

Disadvantages of Investment Bonds may include: -

- The tax advantages only apply for those with marginal rates over 30%.
- Franking credits and capital losses cannot be applied to the individual.
- Limitations to the underlying investments that can be used.

While every care has been exercised and the recommendations and other statements herein are based on information believed to be accurate and reliable, no liability, (unless required by law) can be accepted for any error or omission including negligence however caused.