Orchid Financial Services Ltd

Help-to-buy or lifetime ISA?

A modern-day savings dilemma for many.

Young people in the UK are finding it increasingly hard to save, either for that elusive deposit needed to secure a mortgage on their first home or to fund their retirement.

According to the most recent figures from the Office for National Statistics, between 2014 and 2016, 53% of 22 to 29-year-olds had no savings at all – and that included an Individual Savings Account (ISA).

Figures from between 2008 and 2010 showed that 41% of the same age group had nothing in a savings account, highlighting the number of young people without savings has increased.

An ongoing pay squeeze and the prevalence of increasingly insecure work mean many simply cannot put money aside each month, and that trend extends to some people in their 30s.

Two government schemes aimed to address that in recent years, with the help-to-buy ISA being launched in December 2015 followed by the lifetime ISA in April 2017.

Both products aim to help first-time buyers save for a deposit to buy their first home, although there are several key differences that set them apart.

Help-to-buy

This product is a decent option for first-time buyers looking to save cash for a deposit on a mortgage to purchase a house.

However, if you want one, you only have until 30 November 2019 which is when the help-to-buy ISA will close to new applicants. Existing savers will be able to continue saving as normal.

Most banks and building societies offer some form of access to the scheme, which counts as a cash ISA in terms of your £20,000 annual ISA allowance, and apply their own varying rates of interest.

If you want to open a help-to-buy ISA and you already have an active cash ISA that you're paying into, you will need to transfer up to £1,200 from the cash ISA to the help-to-buy ISA.

Anything more than £1,200 should be transferred to another ISA, such as a stocks and shares ISA, an innovative finance ISA or a lifetime ISA, as you can only save into one cash ISA at a time.

You can kick-start your help-to-buy ISA by depositing up to £1,000 in the first month, with the maximum monthly contribution capped at £200 before interest is applied.

The scheme also enables you to receive a 25% government bonus to boost your savings when you buy a property worth less than £250,000, or £450,000 in London. The maximum bonus you can receive is £3,000.

It's also possible for a couple to double their deposit savings towards securing a mortgage to £24,000 before a maximum government bonus of £6,000 and any interest is applied.

Some 225,618 bonuses were paid through the scheme up to 30 June 2018, which helped 169,980 first-time buyers take their first steps on the property ladder.

The total value of the bonuses paid in since the product's introduction in December 2015 was £189 million, which were used to finance properties worth a total of £29.4 billion.

Withdrawals

You can withdraw the cash you've saved into your help-to-buy ISA at any time, without incurring any exit fees.

The maximum amount you can save in the scheme is £12,000 which, with the maximum government bonus, provides a total of £15,000 towards a mortgage deposit.

When the time comes to withdraw your savings, you have to inform your ISA manager who will then close your account and provide you with a closing statement.

This will not include your 25% government bonus as this is not applied until you complete the purchase of your first home.

Help-to-buy or lifetime ISA?

This means that your solicitor or conveyancer will claim your government bonus sometime between exchanging contracts and completion.

There are some exceptions if you withdraw your money in order to purchase a home and the sale falls through.

Even though you will not be charged for withdrawing your savings, you will not receive the bonus if your withdrawal is for any other reason than to purchase your first home.

If you're buying a home with someone else, you can combine your savings which will include any government bonuses.

Lifetime ISA

You must be an adult and under the age of 40 to be able to open a lifetime ISA, within which there are three options: cash, stocks and shares, or a combination of both.

The maximum amount you can save into this product is £4,000 a year, while the Government pays a bonus of 25% – worth up to £1,000 if you save the maximum amount in a tax year.

The 25% government bonus is available on savings made up until you reach the age of 50, after which age you aren't allowed to pay any more into your lifetime ISA.

There is no official financial limit on how much you can save in a lifetime ISA, although people who start at the age of 18 can save considerably more than those who start nearer their 40th birthday.

For example, an 18-year-old could theoretically save £4,000 every year, plus the £1,000 government bonus, up to the age of 50 giving them a total of £160,000 before interest or investment returns.

However, a 39-year-old who opens a lifetime ISA can only benefit from the government bonus for 11 years which enables them to save up to £55,000.

Withdrawals

The money saved through your lifetime ISA can be withdrawn after the first 12 months, as long as it's to take your first steps on the property ladder.

Several conditions apply if you want to use your lifetime ISA to buy your first home. For instance, the property must be worth less than £450,000 and it must be in the UK.

Like the help-to-buy ISA, you can combine your savings which will include any government bonuses to buy a house with someone else.

If you don't buy a house, you are also free to withdraw after you turn 60, without incurring any penalties. You're also free to withdraw if you have less than 12 months to live.

Savings can be withdrawn before you reach 60 but you face a penalty of 25% for exiting early.

Using both ISAs

The idea of introducing both ISAs was to hopefully encourage you to build up a savings habit for your first home, then, with a taste for saving, carry on afterwards for your retirement.

However, of those who are in the savings habit, many are more tuned in to saving for their first home than saving for their retirement.

That's reflective of the troubles thousands of under-40s face in terms of saving for a deposit to secure a mortgage on their first home.

It is possible to simultaneously save into a lifetime ISA and a help-to-buy ISA – but you may only use the government bonus from one of the products towards your first home.

If you already have a help-to-buy ISA, it is possible to transfer up to £4,000 into a lifetime ISA and benefit from the 25% government bonus in 2018/19 before doing the same for 2019/20.

In circumstances where you have both a help-to-buy ISA and a lifetime ISA, the latter must be invested in stocks and shares as you can only save into one cash ISA in each tax year.

The maximum you can save into a lifetime ISA in a tax year is £4,000, while you can tuck away up to £2,400 into a help-to-buy ISA. The government bonus will only apply to one of these products.

Everyone in the UK can take advantage of the annual £20,000 ISA allowance, so this leaves you with £13,600 of unused ISA allowance to save into other ISAs if you wish.

Speak to us about ISAs.

Important information

The way in which tax charges (or tax relief, as appropriate) are applied depends on individual circumstances and may be subject to future change. ISA eligibility depends on individual circumstances.

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