HB Dobbin
FINANCIAL PLANNING

HELP-TO-BUY ISA: WHAT'S YOUR NEXT OPTION?

Alternatives to make your money work harder.

A few years have passed since the help-to-buy ISA closed to new applicants on 30 November 2019.

Since its launch in December 2015, the scheme offered over-16s a way to save a deposit to help take their first steps on the property ladder.

People could kick start their savings with a maximum deposit of £1,200 in the first month, before paying up to £200 a month thereafter.

Like other ISAs, the savings were held in a tax-free wrapper but they also accumulated interest and a government bonus of £1 for every £4 put in.

This meant first-time buyers could save up to £12,000 into a cash ISA and receive a 25% bonus of up to £3,000 on homes worth up to £250,000, or £450,000 if buying in London.

Around 340,000 buyers took advantage of the scheme before it closed, while thousands of others can continue to save.

With interest rates remaining low and the scheme closing on 30 November 2029, what can you do with your help-to-buy ISA?

BUYING A HOME

The obvious option is to use the cash to purchase a first home, although there is a little-known issue with claiming the government bonus.

If you've saved the maximum into the ISA and intend to use it towards a deposit, the bonus isn't available when you exchange on your purchase.

The bonus is only paid when you complete the purchase. Your solicitor will arrange for it to be paid into your account to help with completion.

Before you reach that point, it might be worth liaising with your vendor's solicitor to see if they would be open to accepting a lower deposit.

Your solicitor would then claim the bonus from the state, before adding it to the rest of your funds to pay the balance when you complete the purchase of your first house.

However, average house prices in the UK hit a record £254,822 in December 2021, according to Nationwide's house prices index.

The typical house is now worth £23,902 more than it was in January 2021, making last year the strongest year for house price rises since 2006.

If you're not ready to buy your first home, or your plans have changed since you started saving into the help-to-buy ISA, there are alternatives.

SWITCH TO A LIFETIME ISA

A lifetime ISA can be opened by anyone aged between 18 and under 40. You can save up to £4,000 a year into it, towards your first home or retirement, and the state adds a cash bonus of up to £1,000 a year on top.

What's more is that the lifetime ISA doesn't have the lower £250,000 house value cap outside London that the help-to-buy ISA has. Instead, the lifetime ISA limit is set at £450,000.

You can save into both a help-to-buy ISA and a lifetime ISA at the same time, although you will only be eligible for the first-time buyers' bonus on one.

Unlike a help-to-buy ISA, a lifetime ISA can be used towards retirement saving and you can invest via a stocks-and-shares lifetime ISA, rather than being limited to a cash ISA.

Another big difference between the two products is that you can put a great deal more into a lifetime ISA and enjoy much larger bonuses, which are paid annually until the age of 50.

For example, if you save £1,000 in 2021/22, you'll have £1,250 and if you save the full £4,000, you'll have £5,000 – and that's before factoring in any interest or growth.

By comparison, the maximum amount you can save into a help-to-buy ISA is £2,400 as the monthly contributions are capped at £200. The maximum £1,000 bonus in lifetime ISAs is also better than the help-to-buy ISA's £600.

Instead of getting the maximum £3,000 bonus when you complete the purchase of your first home with the help-to-buy ISA, you could potentially get a bonus of £32,000 via the lifetime ISA – if you open one at the age of 18 and make maximum contributions until the age of 50.

SHOULD YOU SWITCH?

On paper, the lifetime ISA looks a tempting alternative to the help-to-buy ISA but they might not be right for your circumstances or your long-term goals.

Due to the £4,000 annual contributions cap for lifetime ISAs, you can only transfer up to that amount from other ISAs into this product in any one tax year.

If you switch to a lifetime ISA, you must have held the account for at least a year before you can use the bonus towards your new home. That means it might not be worth switching if you plan to buy your first home soon.

There are age restrictions on opening a lifetime ISA, too. If you're 40 or over, this product simply isn't an option. We can talk you through your options, though.

Also, a 25% charge exists if you make a withdrawal from a lifetime ISA before you're 60 for something that doesn't involve buying a first home. Not only will that reclaim the bonus, it's an extra charge equivalent to 6.25% on your savings.

With a help-to-buy ISA, you can withdraw money – including any interest earned – whenever you want without being charged. You just don't get the bonus.

While it makes sense to switch to a lifetime ISA if you are sure you will buy a qualifying first home worth £450,000 or less, it doesn't necessarily have as much appeal for others, unless you want to use the product as part of your comprehensive retirement savings strategy.

CONVENTIONAL ISAS

Lifetime ISAs count towards your £20,000 annual ISA allowance. So, if you make a maximum £4,000 contribution into a lifetime ISA in 2021/22, you can make contributions into other ISAs of up to £16,000 before 5 April 2022.

Even though interest rates are creeping up in response to rising inflation, cash ISAs continue to offer very little appeal due to the meagre returns on offer.

If you're in your mid to late 30s or early 40s and have a help-to-buy ISA, it might make sense to open a standard stock-and-shares ISA to make your money work harder.

While there's no generous government bonus on offer, you would still be able to benefit from any potential growth and make withdrawals without being charged.

Alternatively, there's nothing stopping you from having more than one ISA at the same time. So, you could have a lifetime ISA for a long-term goal such as saving towards your retirement and a stocks-and-shares ISA for a medium-term goal.

What's right for you all boils down to your own personal circumstances. To understand what the best decision for you is, you might require some personal advice.

Speak to us to work out the best decision for you.