

# CHILD TRUST FUND

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## Introduction

Child Trust Funds (CTFs) were introduced by the Government with effect from 6 April 2005 to help parents save for their children.

Parents who qualify will receive a voucher for £250 (or in some cases £500) issued in the child's name which is to be invested in a Government approved tax-free savings fund. The fund can be invested in cash (ie deposit accounts), bonds (ie fixed interest investments) and equities (ie stockmarket linked investments) over an 18 year period.

Once the child reaches his or her 18th birthday the money can be used by them for any purpose.

Around two million parents with children born on or after 1 September 2002 qualified to receive a voucher at the outset, provided that child benefit had been awarded to them and they lived in the UK. A further 700,000 children now benefit every year.

## Learning about Investing

By providing children with a small amount of capital, a basic understanding of financial products, and some control over their own finances, the Government hopes to encourage future generations to save wisely.

Unfortunately the majority of parents will simply 'invest' the money in a deposit account, which is the most unsuitable type of investment for anyone for an 18 year investment period. The real value of such an investment will be heavily undermined by inflation and will not assist in furthering their child's understanding of financial products.

## CTF Vouchers

Parents who qualify will receive a voucher worth £250. There were slightly higher amounts for children born between 1 September 2002 and 6 April 2005 to effectively add lost interest to the payments.

Lower income families, defined as those where household income does not exceed £14,495 (2007/08) will receive a voucher worth £500.

The voucher must be used to start a CTF account with an approved provider. If the voucher is not used within 12 months the Inland Revenue will open a stakeholder CTF account for the child. These are known as Revenue Allocated Accounts.

When the child reaches the age of 7 the Government will make a top-up payment of £250 directly into the account provided that, at the time, child benefit is still being awarded to them and they still live in the UK. The top-up payment to children from lower income families will be £500.

## Additional Contributions

For parents wanting to make financial provision for their child to go to university, or to help with the purchase of their first home, topping up the CTF account, or regularly contributing to an alternative savings plan over the long term is essential.

According to some estimates, parents will need to save £86 a month from the birth of a child until the child is 18 in order to pay for the average university education.

This figure is based on a growth rate of 6% pa. Even this amount should be reviewed regularly as the cost of a university education rises year on year.

It does not have to be only parents who will be contributing. Family and friends can contribute up to a further £1,200 per year between them to each child's CTF account. This recognises that in many families, grandparents and godparents are likely to want to invest for the child's future rather than buying expensive and possibly unnecessary gifts.

Such contributions can be one off or monthly. It is important to be aware that such contributions are 'locked in' and cannot be returned.

## Tax Situation

In the UK, money saved by a parent on behalf of a child is still treated as taxable on the parent, to stop higher income earners using their children as tax breaks.

Although the child has his or her own personal allowance, any money gifted by a parent will be deemed to belong to the parent unless the interest is less than £100 a year. The only exception to this is National Savings Children's Bonus Bonds.



A major benefit of investing in a CTF is their tax efficiency. Neither you nor your child will pay income tax or capital gains tax on the growth of the investment. Over the years this provides a tax free investment potential of more than £21,000 excluding the growth. This will be of particular interest to high income (and therefore highly taxed) parents.

Once the child reaches 18 the account will cease to be a CTF and the legal title of the investment will be transferred to the child. Earlier access to a CTF account is only possible for cases of terminal illness and death.

You should note that there is no additional inheritance tax (IHT) exemption for CTFs. Top-ups made by parents and grandparents will normally be exempt under the usual small gifts, £3,000 a year, or normal expenditure exemptions. If these exemptions are not available the top-up will be treated as a potentially exempt transfer (PET).

## Types of Account

There are two basic types of CTFs:

-  The stakeholder account is an equity (ie stocks and shares) based product with charges capped at 1.5% pa. There is also an element of risk control with a requirement for 'lifestyling'. This simply means that on the child's 13th birthday equities are progressively sold in favour of lower risk fixed interest and cash investments.
-  The non-stakeholder account is an investment in equities, or a deposit account, or both, but without the 1.5% charges cap.

## Which Type of Account to Use?

The first thing to establish is **your attitude to risk**. As you have no choice but to invest over the long term **you should allow for this and be prepared to take a somewhat higher risk**.

Most parents will no doubt look at the deposit account as being the safe option. Even parents who are happy to invest in equities themselves are often wary of anything which they perceive as risky when it comes to saving for their children.

Parents need to **think seriously, however, about the timescales involved**. One fund management house has recently been quoted as saying that 'leaving the £250 in cash would barely buy a round of drinks on the child's 18th birthday'.

Over the last 18 years a **£250 lump sum placed in a typical bank or building society savings account** at the birth of a child, and allowing all the interest to roll up **would be worth just £557 now**.

The same amount invested in the **FTSE All Share Index would now be worth £1,419**, even after all the market upheaval of 2000 to 2003.







It is a fact that over the last 40 years, **equities have significantly outperformed cash** in every single 18 year period (Barclays Capital Equity & Gilt Study 2007).

A child cannot have a mix of the two but **it will be possible to transfer** from one type to the other or simply because the investment being used is not performing well.

## CTF Providers

At the time of writing there is a full listing of **46 CTF providers** on the dedicated CTF website which you will find at [www.childtrustfund.gov.uk](http://www.childtrustfund.gov.uk).

For parents who wish to use deposit accounts the decision will be a fairly straightforward one. They will want to take account of the rates of interest on offer or perhaps the availability of a branch of the provider in their local high street. Parents who understand **the potential offered by equity linked investments** will want to look at the following:

-  The **Children's Mutual** ([www.thechildrensmutual.co.uk](http://www.thechildrensmutual.co.uk))
-  **F&C Management** ([www.fandc.com](http://www.fandc.com))
-  **Family Investments** ([www.familyinvestments.co.uk](http://www.familyinvestments.co.uk))
-  **Liverpool Victoria** ([www.liverpoolvictoria.co.uk](http://www.liverpoolvictoria.co.uk))
-  **Nationwide Building Society** ([www.nationwide.co.uk](http://www.nationwide.co.uk))
-  **Scottish Friendly** ([www.scottishfriendly.co.uk](http://www.scottishfriendly.co.uk))
-  **Walker Crips Stockbrokers** ([www.wcwb.co.uk](http://www.wcwb.co.uk))

## Risk Factors

- ⊖ Information given relating to Income Tax legislation and Social Security benefits is based on our understanding of legislation and practice currently in force.
- ⊖ Whilst we believe our interpretation of current law and practice to be correct in these areas, we cannot be responsible for the effects of any future legislation or any change in interpretation or treatment.
- ⊖ In particular you are warned that levels of tax and tax reliefs and also State Benefits are subject to alteration and, in any case, the value of such reliefs and benefits may depend on an individual's circumstances.
- ⊖ An investment into a CTF is a long-term investment. It is important that you are aware that the value of units in a unit-linked investment fund within a CTF can fall as well as rise.
- ⊖ Where past performance is mentioned please note that the past is not necessarily a guide to future performance.
- ⊖ These notes are intended as a guide only and do not replace the full product details that accompany each CTF investment.
- ⊖ The present tax free treatment of the benefits may change.

Please note that **this information does not constitute personal advice** and should not be treated as a substitute for specific advice based on your circumstances. If you are in any doubt as to whether an investment in a Child Trust Fund is suitable for your child, then **you should discuss the matter with a suitably qualified independent financial adviser** such as ourselves.

## For Further Info

If you would like to discuss how best to invest in a Child Trust Fund, please ask your usual Arch adviser or contact us via one of the following:

Tel: **0845 3700 661**  
Email: [enquiries@arch-fp.co.uk](mailto:enquiries@arch-fp.co.uk)  
Online: [www.arch-fp.co.uk](http://www.arch-fp.co.uk)

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