THE GOOD GUIDE TO THE INNOVATIVE FINANCE ISA

GOOD WITH MONEY

MORE MONEY, FEWER PROBLEMS

Sponsored by

Lendwise

Invest in education finance & more

Introduction

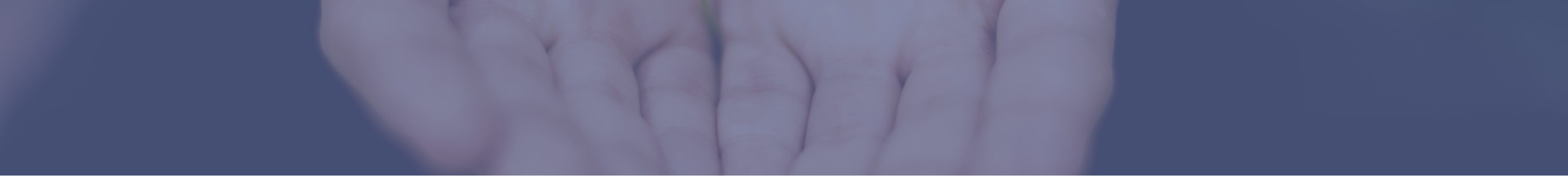
At a time when record-high inflation is eating away at cash interest rates and stock market returns are on (or even below) the floor, investors are looking for smart places to put their cash.

Aside from Cash ISAs and Stocks and Shares ISAs, there is a less well-known kid on the ISA block that's gaining in popularity - the Innovative Finance ISA (or IFISA for short).

According to HMRC, 16,000 new IFISA accounts were opened between April 2021 and April 2022, bringing the total to 142,000 since its launch in 2016. The total invested in IFISAs is predicted to hit £3 billion by the end of the 2022-23 tax year.

Meanwhile, HMRC says Cash ISA deposits declined by £12 billion during the 2020/21 financial year, as consumers rejected the historically low savings rates on offer.

Like the other ISAs, the IFISA is a type of tax-free savings wrapper.
The money you put into one counts towards your overall annual ISA allowance of £20,000 a year.



However, the returns are not like the interest you can get on a cash savings account, nor are they like growth from share prices. Instead, the investments within them are direct loans to businesses, projects or individuals.

If you invest in an IFISA, you are lending money in exchange for an expected (but not guaranteed) return. In general, these loans are riskier than savings accounts, but not usually as risky as investing in individual company shares. The risks are that your capital could be lost altogether, or you may not get back the target returns.

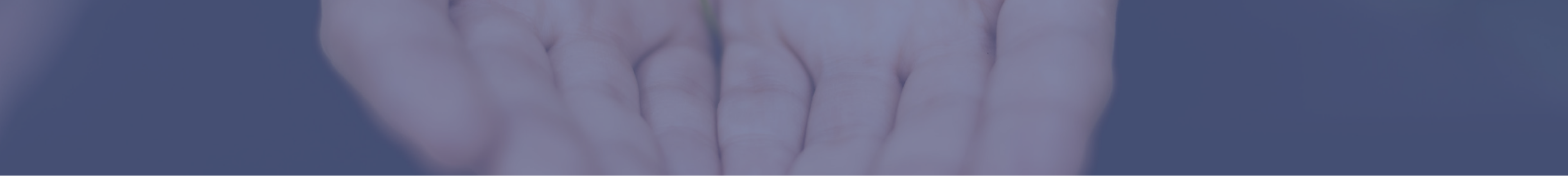
It’s important to note that IFISAs are classed as investments rather than savings. But the risk levels within IFISA investments vary from project to project and business to business.

Some IFISA opportunities offer relatively stable long term returns; others offer higher percentage target returns over a shorter term, but with more risk.

Perhaps it is this variety within the IFISA wrapper that continues to confuse - but this is also the beauty of the IFISA. They are a rainbow product - not at all black and white.

It does mean you need to do your research on each individual offer, though, as they will all have different characteristics. If you would like to see some more variety in your investments they could be for you.

This guide will tell you what you need to know.



What does IFISA stand for?

IFISA means Innovative Finance Individual Savings Account. All ISAs are tax-free savings vehicles. With this one, you can invest in what's called "innovative finance", tax-free.

What is Innovative Finance?

Innovative Finance refers to things like peer-to-peer lending or debt- based crowdfunding. It's called innovative because it is a way of lending to or investing in individuals or businesses, in exchange for a return, which bypasses the banks. The platforms in this space have "innovated" a way to offer more direct, higher paying investments, in other words.

They are also innovative because they have worked out a way for "normal" investors to put money into small and medium-sized businesses (90 per cent of the UK economy), rather than restricting investors to the large multinational companies that make up a typical stocks and shares portfolio.

How is an IFISA different from a normal ISA?

There is no such thing as a 'normal ISA'. Now there are lots of types, all with different characteristics. Stocks and Shares ISAs and Cash ISAs have been joined by Lifetime ISAs, which under 40s can use for either a first home or for retirement; and IFISAs.

IFISAs, like Cash and Stocks and Shares ISAs, have no restrictions on who can invest (see our table on different types of ISA on page 9), but have different characteristics to both.

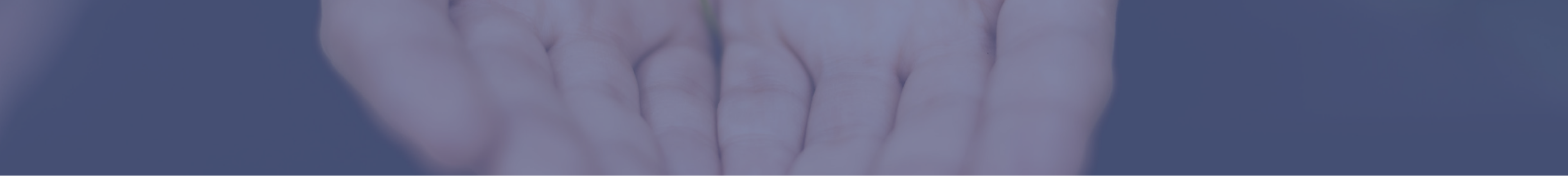
When trying to remember what makes the IFISA special, remember these four I's:

INVESTMENT, not deposit

The most obvious difference between an IFISA and a Cash ISA is that an IFISA typically has a higher rate of return. That's because they are a riskier investment, rather than just a deposit account.

INTEREST, not equity

The main difference between an IFISA and a Stocks and Shares ISA is that Stocks and Shares ISAs allow you to purchase the equity of companies that are listed on an exchange, often via funds, on your behalf, rather than loans or bonds that pay interest.



ILLIQUID, not liquid
Buying equity shares in the stock market means the value can rise or fall in line with the performance of a company, fund or index. You can usually sell your shares at any time, so stocks and shares are considered “liquid”.

With an IFISA, while returns are dependent on company performance, you are lending the money in anticipation of a certain level of interest. Because the IFISA investments are debt-based (so loans or bonds), they are often fixed term. The exception is if you can find someone to buy the loan from you. Many IFISA platforms allow their customers to buy and sell their loans to each other.

INVOLVED, not passive...
Finally, many IFISAs allow you to lend directly to businesses that you choose. This gives you full control over where your money is going.

Why are rates of return on an IFISA typically higher than cash?

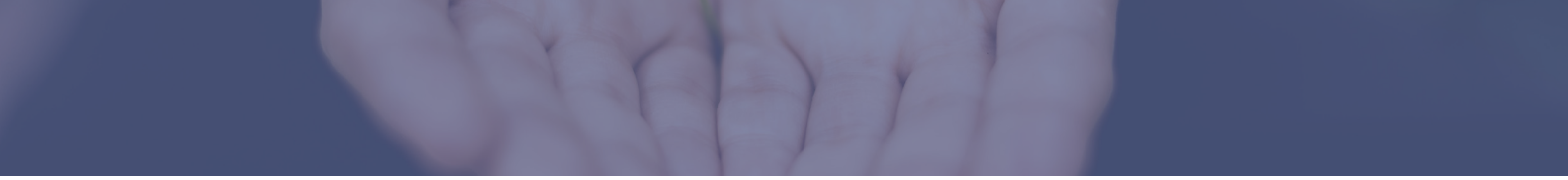
1. There is always the risk that a company could fail, for whatever reason, even if its historical cash flow has indicated a decent credit risk. The risk of failure of the company or the individual that you are lending to is one reason for the higher return. Bear in mind that the nature of the risk can vary between companies or projects, even when returns are similar, so it’s always worth checking the Offer Document.

2. Lower overheads than some traditional platforms. Innovative finance platforms do not have large networks to support. In theory this means they can pass on the savings from lower overheads to customers, in the form of higher returns.

3. Lower fees. Partly because of the lower overheads, innovative finance platforms can afford to operate on lower profit margins than older businesses, so they can also afford to charge lower fees for arranging finance deals between lenders and borrowers than banks.

Why would I invest in an IFISA rather than a normal ISA?

It’s difficult to give a general answer to this question, as it would depend on the type of loan you are making and also on the type of borrower. Compared with Cash ISAs, IFISAs have the advantage of typically higher returns. This is especially true now when inflation has passed an eye-watering ten per cent, meaning that your cash savings are depreciating



in value significantly, just by sitting there. However, IFISAs are also riskier than cash. Rising interest rates this year may also begin to dampen down inflation and improve the returns available on cash in the coming months. Higher interest rates might also further improve rates of return on IFISAs.

IFISAs have, on average, produced higher returns than many Stocks and Shares ISAs. Research by Peer2Peer Finance News found that **IFISAs outperformed the UK FTSE All-Share Index** (made up of the FTSE 100, FTSE 250 and FTSE Small Cap companies) during the four years from 2018 to 2021, with average returns of between 7.8 and nine per cent per year.

You might choose an IFISA to complement a Stocks and Shares or Cash ISA you hold, rather than replace them altogether. In fact, many investors open IFISAs as a way to diversify their other investments.

For instance, a stock market investor worried about a downturn in equity markets might put some money in an IFISA, which is not tied to stock market performance, to hedge against a slump.

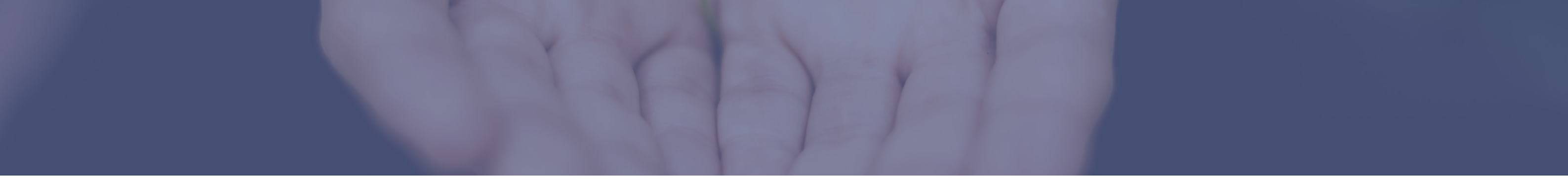
This could be particularly useful for someone investing tax-free for the long term. This might include retirement saving, for example, as well as those wanting to use ISAs alongside their pension pots.

Be mindful, however, that some businesses or sectors borrowing via peer-to-peer platforms will be affected by tricky market conditions.

How much can I put in an IFISA?

You can put up to £20,000 in any type of adult ISA in a tax year (April 6 to April 5). So you could put all of this into an IFISA, or you can split it between different kinds of ISA if you wish. But £20,000 is the annual tax-free maximum.

£20,000 ISA limit per tax year



For example:

Mrs King is 36 and wants to take advantage of the Lifetime ISA for her retirement savings. She also likes the idea of an IFISA, because she has found a community energy company offering a seven per cent bond. She has £10,000 to invest in this tax year. The maximum she can put in her Lifetime ISA is £4,000. She chooses to put the remaining £6,000 in an IFISA.

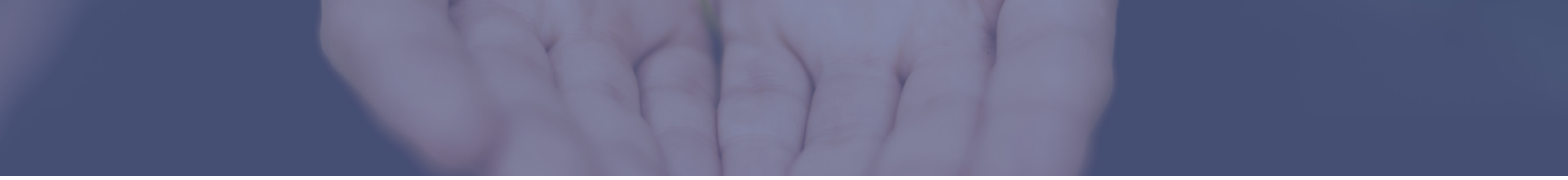
A Cash ISA investor curious about IFISAs might choose to set aside a small amount in an IFISA to bring a little more income to their investment portfolio, without sacrificing more security than they are comfortable with. ... And some might say the IFISA is more interesting, because it allows you to choose businesses you think look like good investments directly – and to choose investments you really like.

Why are IFISAs riskier than cash?

The important advantage of Cash ISAs is that unless the bank or building society goes bust, you know you will get the quoted interest rate. With IFISAs, it's not so simple. If you are lending to a group of individuals, there's a bad debt risk that may bring down your rate of return.

If you are lending to a business or project, there's also a risk that the business might not hit its targets and so will not be able to return the quoted figure to you.

Cash ISAs with banks or building societies are covered by the Financial Services Compensation Scheme. If the bank fails, deposits are protected



up to £85,000. It is important to realise that there is no such cover for investment-related losses.

It is now mandatory for peer-to-peer platforms to have a 'Wind Down Plan,' setting out an effective wind down of their loan book in case they are no longer able to serve new customers.

In the event of a platform failure, in some cases a third party might step in to manage the loans, so that investors do not lose out.

Often there is some kind of insurance cover that would pay out in case a borrower was unable to repay lenders. But if there isn't any kind of cover for lenders with your IFISA, you run the risk of not getting your capital back at all and certainly the risk that your returns will not be as high as expected.

How can I tell how risky an IFISA is?

Generally speaking, the higher the rate of return, the higher the risk level. You should always research the particular risks of what you are investing in. You may decide, on further investigation of a higher rate offer, that the specific risks involved are risks you are prepared to live with.

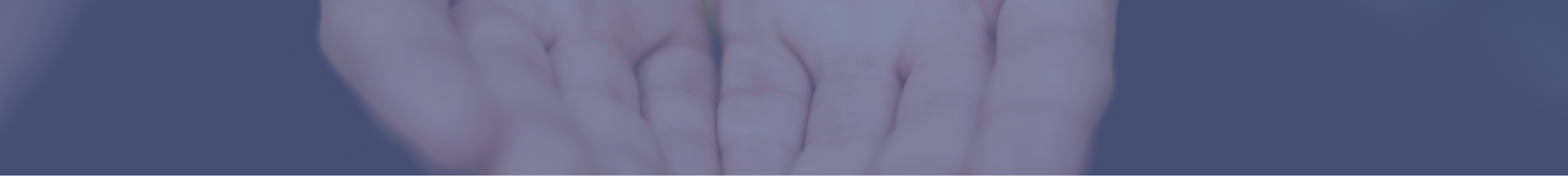
Platforms should have information on their website that clearly sets out what the risks associated with their specific investments are. They will also usually state how much due diligence and credit checking they perform, but should be happy to answer questions directly.

In August 2022, the Financial Conduct Authority brought in tougher rules for the marketing of "high risk" investments such as peer-to-peer lending to ensure that consumers are aware of the risks before investing.

Has anybody actually lost money through IFISAs yet?

The major UK-based IFISA providers generally have a good track record in protecting savers' money, but yes there have been cases of people losing out.

London Capital & Finance was an IFISA eligible lender offering mini-bonds, which collapsed in 2019. Many people at first lost all of their investment, though some received compensation. However, in this case the Treasury later opened a compensation scheme because of regulatory failings.



Other peer-to-peer lending platforms have closed in the years since the IFISA was introduced and some people's IFISA investments have not performed as hoped, leaving them with lower returns. One of the biggest peer-to-peer lending platforms, Ratesetter, sold its loan book to Metro Bank last year.

It is important to note that there is no Financial Services Compensation Scheme protection if a peer-to-peer platform fails. However, as mentioned above, all platforms must have a Wind Down plan clearly showing how they would cease to conduct regulated activities while causing minimal harm to clients, partners and the markets.

What is the average default rate for peer-to-peer lending?

The key risk in peer-to-peer lending is that a person your money is being loaned to may default on their repayments. Default rates can vary widely between platforms, so always check before you invest.

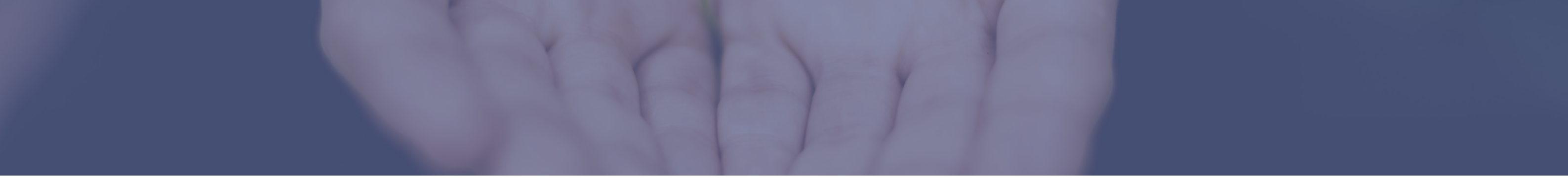
It is always wise to diversify your investments so you are lending to multiple borrowers.

Can I invest with different IFISA platforms in the same tax year?

Unfortunately, you can't. All of your IFISA money has to be held with the same platform in that tax year. There's nothing to stop you shifting your IFISA pot between different platforms once a year, but you can't contribute to more than one at a time.

Can I transfer an existing ISA into an IFISA and vice versa?

Transferring your existing ISA funds into an IFISA is really easy. You can find a form on the platform you want to transfer your funds to. Print this off, fill it out and send it to the NEW platform at the address provided. They will then instruct your OLD ISA provider to move the funds across.



What are the different types of ISA?

	Limit	Risk level	Typical interest/return	Features
Cash ISA	£20,000	Low	Low <1.5%	Allows savers to deposit savings up to the annual limit in accounts covered by the Financial Services Compensation Scheme.
Stocks and Shares ISA	£20,000	Low to high depending on type of fund or shares held	Varies depending on risk level, performance and fees. Equity not debt and therefore capital growth rather than interest	Up to £20,000 can be mix of stocks and shares and cash, can be “flexible” so you can take money out and put it back in without losing the tax-free status of that bit of your allowance.
Junior ISA	£9,000	Low to high depending on type of fund	Varies depending on risk level, performance and fees. Capital gains rather than interest	Cash or stocks and shares or a combination of the two. In the child’s name so does not form part of your £20,000 annual allowance. The child can access the pot when they reach 18.
Innovative Finance ISA	**£20,000**	**Medium to high depending on diversification/ interest rate**	**Varies – around 5-8%. Debt-based, therefore pays interest not capital growth**	**Introduced April 2016. You can have multiple IFISAs but all new contributions in a single tax year must go into the same IFISA.**
Lifetime ISA	£4,000 (this counts towards your annual £20,000 ISA limit)	Low to high (cash or stocks and shares)	Varies depending on type/risk level, performance and fees. Equity not debt, therefore pays capital growth not interest	Government will top up annual savings of up to £4,000 with a 25% bonus (so a maximum of £1,000 per tax year). You must be aged 18 to 39 to open a LISA and the government will pay the bonus until you are 50. Savings in the LISA must be used to either buy a first home or towards a pension. Pension can be accessed from age 60. Part of annual £20,000 allowance.

By Lori Campbell,
Editor of Good With Money

How higher education can pay off - for students AND investors

Higher education gives a boost to an individual's earning potential and job prospects - but it can also pay off for investors.

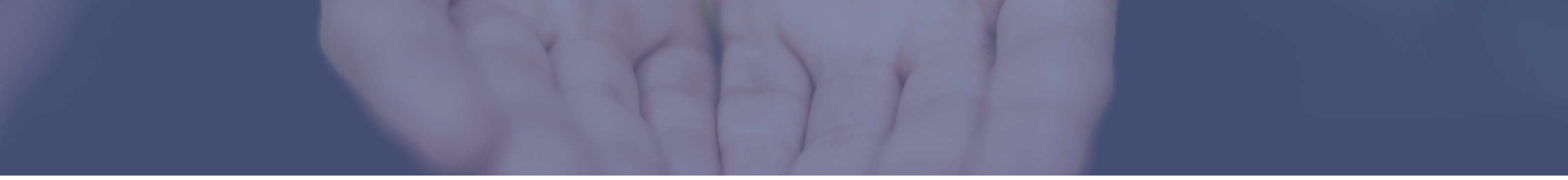
Postgraduate students can find it difficult, or even impossible, to get affordable funding for their course from traditional high street banks and Government-backed loans often don't stretch far enough to cover personal expenses on top of tuition fees.

Lendwise, which launched in 2018, aims to fill this gap by matching investors with borrowers who want to fund their studies to further their career and therefore their earnings potential. It is the UK's only peer-to-peer lender to specialise in education finance.

The platform provides fair and flexible loans to students who have the personal merit to take postgraduate courses at top business schools and universities in the UK or internationally - but maybe not all of the funding.

Meanwhile, lenders can target a competitive return on their investment of around six to 12 per cent while also making a positive social impact.

Lendwise co-founder Kypros Mouzouros said: "We strongly believe that if you are smart enough to go to university, and you have shown the



aptitude and the application in your studies, a lack of funding should not stop you from pursuing your aspirations further.

"That is why Lendwise exists - to help those who want to keep learning to be able to do so without burdening them with unfair loan terms.

"On the other side of this, we offer an attractive opportunity for investors who are looking to make a personal profit and a positive difference to society at the same time."

How to invest with Lendwise:

1. Before you start investing with Lendwise, you'll be asked to take an 'investor appropriateness test' to determine what kind of investor you are and how much risk you can afford to take and are comfortable with.

2. Then, you'll need to open an IFISA account and fund it with a minimum initial investment of £1,000 (If you choose a Classic account, which comes without the tax benefits of the IFISA, the minimum is £200).

3. You can either manually choose the loans you want to fund (it's wise to spread your investments over multiple loans - see below), or use Lendwise's 'AutoLend' feature to do this automatically according to your appetite for risk and investment objectives.

4. You will receive capital and interest repayments monthly in line with when the borrowers you have funded are paying off their loan (this may start up to six months after they graduate).

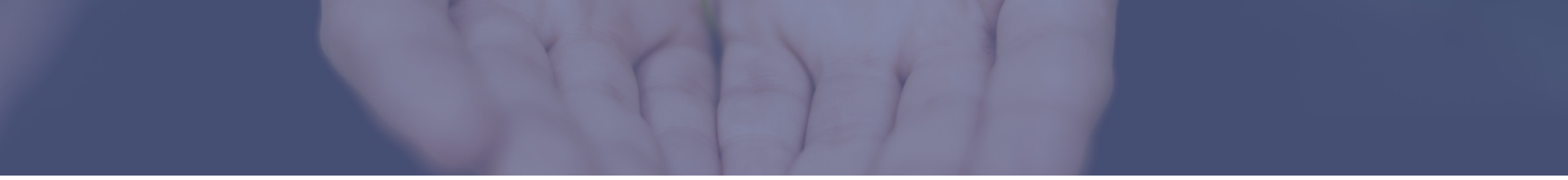
5. This money can either be reinvested, or withdrawn as cash.

What's the risk?

To keep risk as low as possible, Lendwise has strict criteria for its borrowers. The platform analyses a student's future earnings potential, according to their chosen career, as well as their financial history and creditworthiness before offering them a loan.

Kypros said: "We are very cautious about the students we lend to, and in doing so believe the risk can be lower than with other types of investments. Afterall, Lendwise is the only loan of this type that actually enhances a borrower's ability to repay it over time.

"The main risk with Lendwise is that a student may default on their loan, but thanks to our thorough application process the number of defaults we have is very low - currently under two per cent."



Lenders are advised to split their investments across multiple individual borrowers in varying study areas and graduating over a number of years. This helps to diversify their lending portfolio and reduce risk.

Kypros said: “For example, a £1,000 investment might be split across 100 loans at £10 each. This way, if one or two borrowers default, the impact on the overall portfolio return will not be significant.”

Lendwise aims to help both borrowers and investors to achieve their goals. “For students, access to affordable education finance means they can fulfil their academic and career aspirations, which in turn leads to higher income and benefits the economy,” said Kypros.

“At the same time, investors can directly access a socially responsible investment opportunity that aims for strong financial returns.”

** As with all forms of investment, your capital is at risk. Investments on the Lendwise platform are not covered by the Financial Services Compensation Scheme (FSCS). Investment returns on the Lendwise platform are not guaranteed and past performance is not a reliable indicator of future performance.*

Lendwise
Invest in education finance & more

By Lendwise

Making a social impact with your IFISA

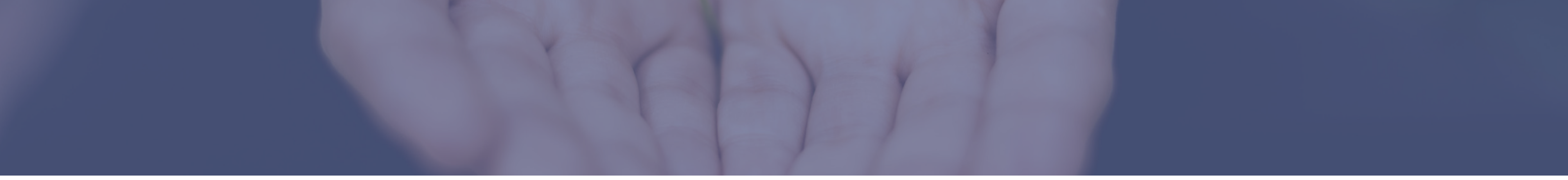
The money in your IFISA has the potential to make a powerful social impact alongside a personal profit.

Peer-to-peer education finance helps students - who can find it impossible to get affordable credit elsewhere - to achieve their academic and career goals, while also improving their chances of earning a higher future income.

Lendwise chief executive Rishi Zaveri said: “Myself and my two co-founders, Yiannis Georgiou and Kypros Mouzouros, wanted to do something not only entrepreneurial, but something that had this aspect of making a difference to wider society. Enabling access to education is very much something that ticks that box for us.”

Zaveri says that the platform’s commitment to doing social good is already paying dividends.

Investors have historically received average returns of up to nine per cent per annum. Alongside this, in the four years since the platform has been originating loans, Zaveri has received scores of emails and messages from former borrowers thanking the company for the opportunities that their Lendwise loan has given them.



“We’ve had some lovely emails and feedback from so many of our customers who are very magnanimous when they say that were it not for the loan from Lendwise they wouldn’t have been able to achieve the outcomes that they have been able to achieve,” says Zaveri.

“It’s not the loan in terms of just the money, but the loan in terms of just the way that the product works, in terms of the fact that there’s no repayments while you study, the flexibility of being able to repay your loan early or make overpayments without having any penalties or charges, but at the same time having an interest rate fixed.

“And that’s the social impact right there.”

Lendwise offers education loans to graduates who are keen to improve their earning potential and make a difference in the wider world. Former borrowers have gone on to become doctors, nurses, academics, teachers, engineers and even financing specialists themselves. By making fairly-priced loans available to graduates, Lendwise is creating social opportunities for its borrowers.

“Your investment is going towards someone who is, in a way, investing in themselves,” says Zaveri.

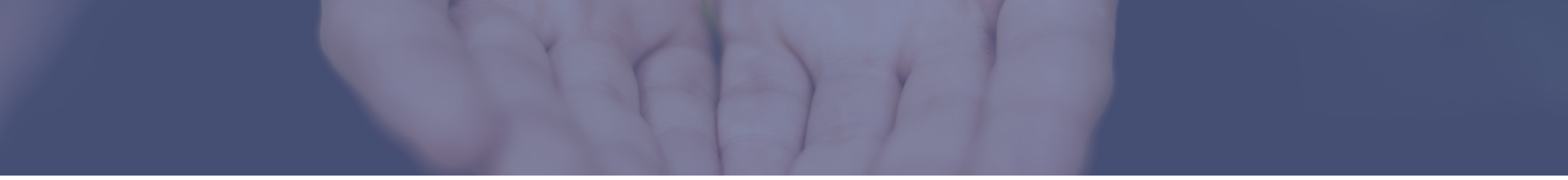
“They are pursuing postgraduate education, which is either augmenting their skills or they’re reskilling. But either way, they are doing something that will have a positive outcome in the sense of a better salary and better career progression.

“We’re all about outcomes,” he adds. “It’s not for us to say who should study what and where. We’re inclusive as a platform. What we want to see is that by undertaking a form of education, there’s an outcome that’s being attained which is enabling someone to go on and do better.”

Lendwise’s credit committee is where loan applications are analysed, assessed and discussed. Once a credit decision is made, the platform generally only communicates with a borrower if there is an issue with any repayments. However, Zaveri notes that the platform has a 96 per cent on-time collection rate, which means that borrower interventions are minimal.

In the future, Zaveri is keen to change this and follow up with more former borrowers to learn more about the various ways these funds have benefited individuals and the wider community.

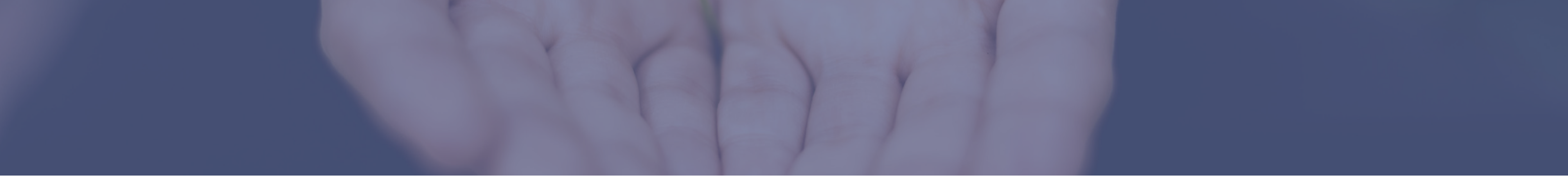
“It’s really heart-warming to hear from our former borrowers,” he says. “And actually, it serves as a nice reminder that there is a wonderful impact we’re having on our customers.



"But let's not forget our lenders, who are the ones truly making all of this possible. They are delivering that impact by investing in these loans whilst earning a commercial return.

"They should be very proud of the social impact that they have had and are continuing to have by investing on Lendwise."

*Content in this article first featured in **Peer2Peer Finance News***



Is an IFISA right for me?

Do you already have an ISA?

YES → Are you happy with your returns?

- YES / NO → *"NO" or "YES" - if your returns are lower than 5 per cent, you stand to make higher gains through an IFISA*

Would you consider moving your existing ISA pot?

- NO → Why not?
  - *- Hassle*
  - *- Exit charges*
  - *- Happy with existing platform*
  - *- Happy with existing returns*
- YES

NO → Would you like to start one?

- NO
- YES

Are you prepared to accept a little more risk for higher returns than cash savings?

- NO → *If you do not want to take a risk with your capital, you should seek the highest interest Cash ISA or savings account you possibly can and try to ensure that it is at least covering inflation*
- YES

Are you prepared to diversify your own ISA portfolio?

- NO → *It is possible to diversify your own IFISA portfolio. However if this is not for you, you would probably be happier investing in funds within a Stocks and Shares ISA, where fund managers diversify for you (for a fee)*
- YES

Would you like your money to be invested directly into British businesses.

- NO → *If you don't want to invest directly into companies, you might want to consider funds within a Stocks and Shares ISA*
- YES

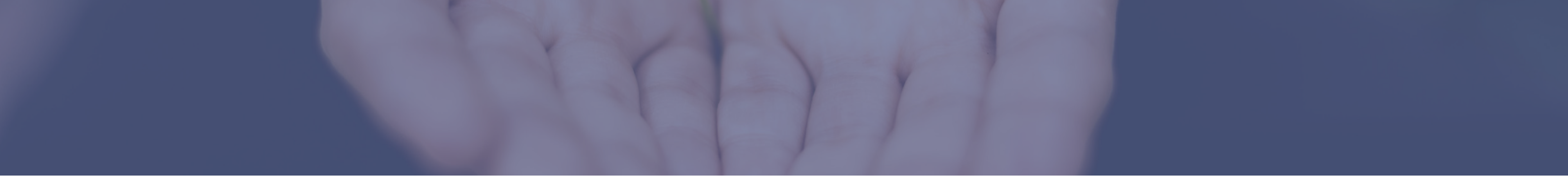
Have you got a £1,000 deposit to invest?

- NO → *IFISA platforms such as Abundance and Triodos Crowdfunding have lower minimum investments. However, to really notice the benefit of interest adding up, it makes sense to invest the maximum you can manage (as a one-off deposit and/or monthly contribution) to your IFISA.*
- YES → *You could invest in Lendwise or any of the regulated IFISA platforms.*

Would you prefer to lend to individuals (such as for education) or a range of businesses?

- Education → Lendwise*
- Tackling climate change → Abundance
- Range of innovative businesses → Ethex, Energise Africa, other IFISA platforms
- Renewables and social enterprises → Triodos Crowdfunding
- Personal loans → Lendable, Fast Invest

* Plans to launch personal loans in late 2022



How to choose a platform

As you can only invest in one IFISA in a tax year, it might take you a while to decide which one is for you and you should consider how your IFISA will fit within your wider portfolio. If you invest a lot in buy-to-let property, for example, you may prefer to lend to individuals or businesses instead.

There are now a whole host of different IFISA platforms to choose from, all offering something different for interested investors.

Most will help you to open an IFISA and then you can choose which bonds from their platforms you would like to place inside it, up to your annual limit.

The Lendwise platform enables you to make a commercial return whilst making a real difference to wider society.

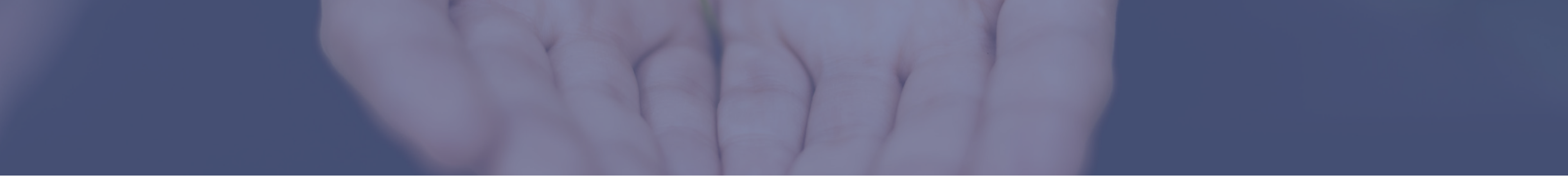
By investing in higher education loans, you are removing the financial constraints for ambitious and talented students, therefore helping them to achieve a better life through higher earnings arising from postgraduate education.

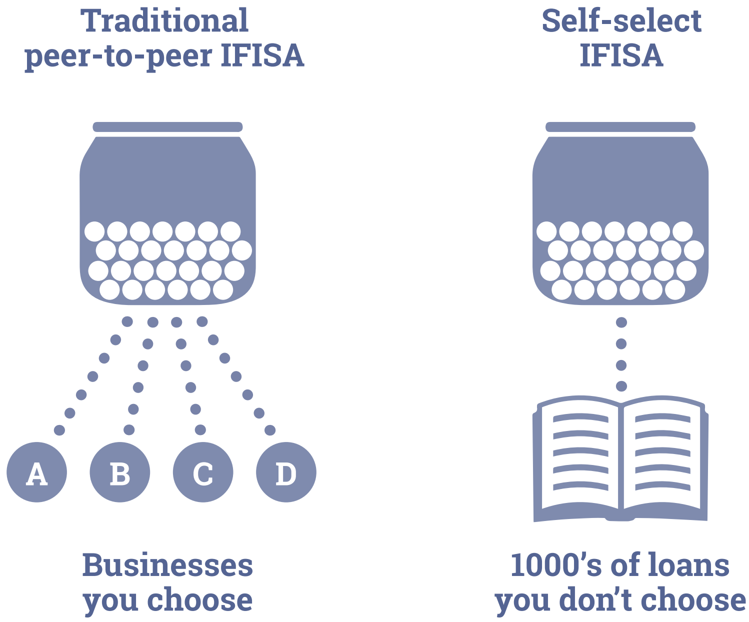
Platforms like **Ethex** help everyday people make ethical investments that fund businesses doing something extraordinary for other people or the planet.

This includes Solar for Schools which works with schools and communities to deliver carbon and cost savings with solar energy. Or Bunker Housing Co-operative, which is helping to tackle the housing crisis in Brighton and Hove.

You might prefer to lend to organisations in the developing world, and **Energise Africa** provides such investment opportunities. For example, helping Sollatek provide clean energy to homes in Kenya or Solarise to install solar home systems in businesses across Sub-Saharan Africa.

Other IFISA platforms and providers include **Triodos Crowdfunding** for investments in positive impact businesses, **Abundance Investment** for renewable energy investments.

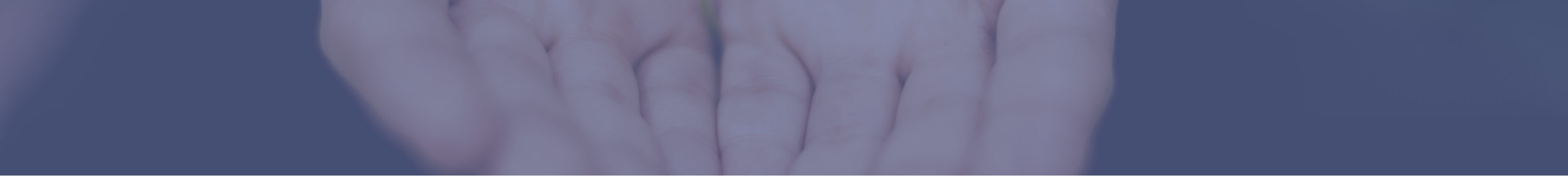




With these options, you know exactly where and who your money is going to. It is still important, however, to manage your risk by investing in a wide range of businesses.

Things to remember

- As long as you don’t invest more than £20,000 in a tax year, your earnings will be tax-free.
- You can have multiple IFISAs - and transfer money into them from existing ISAs. However, you can only put new contributions into one IFISA in the current tax year, with one provider.
- You can use your annual ISA allowance across a combination of Cash or Stocks and Shares, Innovative Finance or Lifetime ISAs.
- The £4,000 maximum you can put in a Lifetime ISA is part of the £20,000 maximum, so you still have £16,000 to invest or save tax-free before you reach the limit.
- You can invest lump sums or monthly in all ISAs.



About Good With Money

Good With Money is a money website with a difference: it is all about how your money can do more good for people and planet, as well as line your pocket.

It created the Good Egg mark, a licence for financial services companies that make a positive impact.

Sign up to the weekly newsletter for the latest good money tips, reviews and inspiration **here**.

About Lendwise

Lendwise is the only peer-to-peer lender in the UK dedicated to education finance, allowing ambitious individuals to improve their career potential and future earnings.

Investors with Lendwise have enabled students to study at universities and business schools across the globe, therefore making a positive social impact while also targeting a personal financial return.

Lendwise directly addresses two of the United Nations’ Sustainable Development Goals - Quality Education and Reduced Inequalities.

Lendwise is authorised and regulated by the Financial Conduct Authority. You can find out more at **https://www.lendwise.com**.

CONTACTS

Good With Money
Editor: Lori Campbell
lori.campbell@good-with-money.com
www.good-with-money.com
@GoodMoneyGirl

Lendwise
https://www.lendwise.com