Adviser Q&A

Star Letter

What challenges and opportunities has the recent reduction in the lifetime allowance given advisers when having protection conversations with their clients?

(Martin Byrne, Owner, Business Protect Ltd)

With Johnny Timpson, Scottish Widows

Good question. In April 2016 the lifetime allowance (LTA) reduced for the third time in four years to £1m. As a result, an increasing number of high earning clients entitled to group life cover as part of their employee benefits package could now unwittingly face a tax charge, despite holding pension funds valued below the LTA. Appropriate advice and relevant life cover could help overcome this risk, and provide additional benefits.

Larger employers offering death-in-service benefits have historically chosen to provide this via a registered group life scheme alongside their occupational pension scheme. However, as pension legislation applies to registered group life schemes, this means that payable benefits are assessed against the employee's LTA and a tax charge of up to 55% will apply if the limit is breached.

Swiss Re's recent Group Watch 2015 report illustrates that many employers are now setting up standalone 'excepted' group life cover under a separate trust, as the number of people insured under such arrangements in 2015 has increased by 25% compared to 2014. If an employer has excepted group life or relevant life policy provision in place then neither the LTA nor any potential annual allowance problems apply. Therefore, advisers can add value by drawing high-earning clients' attention to this issue and make sure they check the basis of any death-in-service provision with their employer. Swiss Re's research also highlights a further trend: a 14.1% reduction in the provision of in-force widows' and dependents death-in-service pension provision. This decline is likely to accelerate with the closure of more of the remaining defined benefit pension schemes. This, along with the scheduled reform of working age welfare bereavement benefits expected to come into effect in April 2017, offer good reasons to discuss the benefits of appropriate death-in-service cover provision.

A relevant life policy (RLP) can be a suitable solution to allow an employer to set up life cover that is tax efficient, as long as the benefits are payable to an individual or charity and cover ceases by age 75. Premiums paid by the business are an allowable deduction against corporation tax, and there is no national insurance liability for either employee or employer. As an RLP is typically set up as a discretionary trust established by the employer as settlor, the policy doesn't belong to the employee. So where a claim arises the proceeds should fall outside their estate for inheritance tax purposes. Note, however, that periodic and exit charges of up to 6% can apply in exceptional circumstances.

RLP can also be an attractive option in a number of other situations:

- Small family-run micro businesses and/or SMEs may have too few employees to be eligible for an excepted or registered group life scheme.
- An employer may wish to provide additional, bespoke cover to certain high earning employees than provided under its group life scheme. An RLP could sit alongside an excepted or registered group life scheme to achieve this.
- It's not possible to write a group policy on a single life basis. A key advantage of an RLP is the ability to tailor and precision engineer benefits for an individual employee – this may not be possible with an excepted or registered group life scheme.
- An employee has pension savings with enhanced or fixed protection as they would be unable to join any new registered group life scheme as this would result in protection being lost.
- Portability is a consideration, as by including the employee as a potential beneficiary of the relevant life policy trust, cover can continue where an employee ceases employment with the employer. Under a group life scheme cover would cease on leaving employment, resulting in the need for fresh underwriting where a requirement for cover via an individual policy remained.
- A provider may be able to offer a central collection facility whereby contributions are collected for all its RLPs together, creating, in effect, a mini group scheme but with benefits tailored for each life assured.

As we have seen, there is a real opportunity for intermediaries to have conversations with clients around whether they have appropriate death-in-service cover in place, with relevant life a strong contender for providing a solution that is tax efficient, and can help minimise unnecessary tax charges.

Source: Swiss Re

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