AIG Life

Relevant Life Insurance
A guide for employees and small businesses

Life insurance as an employee benefit

If you own, run or work for a small business, you can get life insurance without paying more than you need to.

Life insurance is a valuable employee benefit which many people get through their employer's group life insurance scheme. HMRC supports this provision with tax relief for both the employee and the business.

Smaller-sized businesses - usually those employing five people or less - are not usually large enough to run a group life insurance scheme. For employees of such businesses, this means the employee either has to take out insurance and pay for it themselves (so does not benefit from any tax savings) or does not make any provision at all and therefore has less life insurance than they might need.

So how can you ensure sufficient coverage outside of a group scheme?

That's where relevant life insurance comes in.

What is relevant life insurance?

Relevant life insurance is a form of life insurance for an individual employee.

The policy is applied and paid for by the business, and is written into trust so it pays out a lump sum to the employee or their beneficiaries if they die or are diagnosed with a terminal illness while employed during the policy term.

It's covered by legislation which means that, in most cases, premiums (the cost of the insurance) are viewed as an allowable business expense by HMRC, making it a smarter way to get life insurance. The business pays the premiums but they'll cost much less than taking out a personal policy.

How does it save on the cost of life insurance?

The legislation covering relevant life insurance means it is:

- TAX-EFFICIENT FOR THE EMPLOYEE BECAUSE
  HMRC usually views the premiums as an allowable expense for the employer. It is not seen as a benefit-in-kind for the employee, so the employee does not have to pay Income Tax or National Insurance on the premiums. This can be a significant saving for a higher or additional rate taxpayer.

- TAX EFFICIENT FOR THE BENEFICIARIES BECAUSE
  the policy is set up using a split trust. Any payout will also be received free of income tax as well as, usually, any Inheritance Tax liability.

  Importantly, unlike group life insurance, relevant life insurance is a 'non-registered' arrangement so any payout does not count towards the employee's lifetime pension allowance. Therefore, the family will not have to pay tax on any lump sum payment in excess of the lifetime allowance when they come to claim on the employee's relevant life insurance.

This can be a significant consideration for employees who may be near the limits of their lifetime pension allowance.[1]

1 The lifetime allowance is the maximum amount (£1 million for tax year 2016/2017) of pension saving 'pot' you can build up over your lifetime and that benefits from tax relief. Any lump sum payments under a registered scheme fall into this pot. The rate of tax you pay on pension savings above your lifetime allowance will depend on how the money is paid to you: this will be 55% if you get it as a lump sum or 25% if you get it in any other way, e.g. pension payments or cash withdrawals.

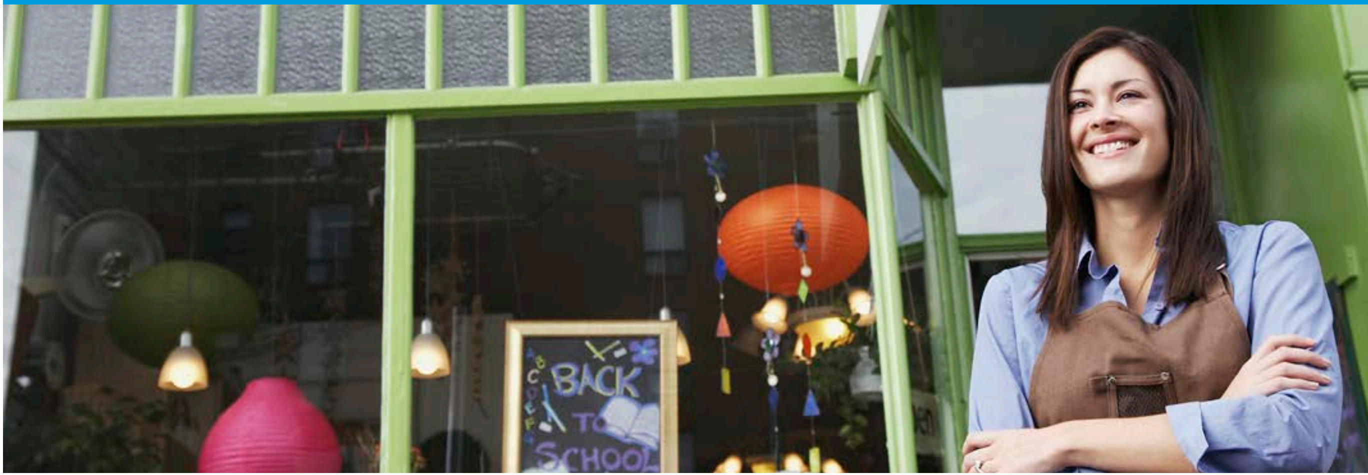
- TAX-EFFICIENT FOR THE BUSINESS because as long as the local inspector of taxes is satisfied that the insurance premiums are 'wholly and exclusively' for the purpose of trade, the premiums should be treated as part of the employee's remuneration package, this represents not only cash but other benefits as well, such as death-in-service or pensions.

  Therefore, the payments may be an allowable expense in calculating their tax liability which means the business can claim tax relief.

Who is relevant life insurance suitable for?

Relevant life insurance may be suitable for:

- Businesses that do not have a group life scheme, but want to provide life insurance cover for individual employees which pays out if that employee dies or is diagnosed with a terminal illness while in employment, up to age 75.



- 'Employees' must be aged 17-71 when the insurance is taken out and can include directors on PAYE and single directors of a limited company (for example management consultants, IT contractors, etc.).

- Businesses that do have a group scheme, but who wish to provide their high-earning employees with additional life insurance that does not count towards any of their annual or lifetime pension allowances.

- Employees who want the business to top-up the life insurance benefits they get from their employer's group life scheme (a group life insurance scheme usually only covers up to 4 x salary, whereas Relevant Life Insurance from AIG can cover up to 30 x salary, depending on age).

Who is it not suitable for?

Relevant life insurance is not suitable if:

- There is no employer-employee relationship between the cover owner and the person covered. For example, we cannot insure a sole trader (in their capacity as business owner), an equity partner of a partnership relationship or an equity member of a Limited Liability Partnership who is taxed as self-employed;

Relevant life insurance - valuable life insurance as an employee benefit

- You want to insure a business loan, shareholding in a business, a key person, or otherwise intend for the payout to benefit the business;

- You want it primarily to avoid taxes or for the benefit of the business (we would be concerned that these rules were being compromised if the payout was intended to go to business beneficiaries such as a co-shareholder or an organisation other than a nominated charity);

- You want an insurance that includes other benefits (critical illness, disability, waiver of premium) or has a surrender value;

- The employee is not aged 17-71; or

- You want insurance that extends beyond the age of 75 or while not in employment.

What happens if the employee leaves the business?

We can simply transfer the policy to a new employer, provided the new employer agrees and is happy to pay the premiums. A new trust will need to be effected (with the new employer and employee as trustees; it may also be beneficial to appoint a further trustee).

Alternatively, the insurance can be transferred into the sole name of the employee. The employee would be responsible for paying the premiums going forward. The existing trust would cease to exist and the terminal illness benefit will be removed from the policy. Furthermore, the employee may no longer qualify for the tax benefits associated with this policy. The employee should consult their financial adviser for professional advice before exercising this option.

Note that the transfer has to take effect within 90 days of the employee leaving their previous employer.

How much could it save?

Helen Thomas is a founder and managing director of a user experience design consultancy in London. She works full-time and her company employs two designers - Bethany and Ross.

After leaving her previous employer and setting up her own company, Helen has lost her death-in-service benefit. Her financial adviser suggests she purchases life insurance through her company, and after comparing relevant life insurance to a standard life insurance, it appears relevant life insurance is a more beneficial option for Helen.

Example: Company Director

The cover that Helen needs requires a premium of £83.33 per month. She is a higher rate taxpayer (40%) and pays National Insurance at 2% on the top end of her income. The company pays National Insurance at 13.8% (this assumes that the employee is not contracted out of the Additional State Pension). Corporation Tax is calculated at 20%.

In the illustration of the cost of non-relevant life insurance below, it is assumed Helen's company pays the premium under insurance that Helen proposes for herself, as an employee.

		Personal life insurance	Relevant life insurance
		Helen	**Helen**
Cost to **employee**	Monthly premium (from net salary)	£83.33	£83.33
	Employee national insurance contribution (@2%)	£2.87	n/a
	Employee income tax (@40%)	£57.47	n/a*
	Total cost to employee**	**£143.67**	**n/a***
Cost to **employer**	Monthly premium	n/a	n/a
	Employer national insurance contribution (@13.8%)	£19.83	n/a
	Total gross cost	£163.50	£83.33
	Less corporation tax (@20%)	£32.70	£16.67
	Tax adjusted total cost	**£130.80**	**£66.66**

By opting for relevant life insurance, Helen's company is saving a total of £64.14 (49%) per month which is £769.68 per annum

* The payments employers make are not subject to Income Tax because they are not normally assessable on the employee as a benefit in kind.

** These are the gross earnings required to leave sufficient net income to pay the premium. By providing relevant life insurance for the employees, the benefits will not form part of the employee's lifetime pension allowance and the payments made will not form part of the employee's annual tax allowance.

Example: Small business

Digital design is a competitive market so Helen wants to ensure that she employs the best people and offers attractive employee benefits, including life cover. However, as her company is relatively small, a group scheme is not an option, so Helen's financial adviser suggests relevant life insurance.

The two employees she would like to provide cover for are Bethany and Ross. They are both higher rate taxpayers (40%) and pay National Insurance at 2% on the top end of their income. Their employer pays National Insurance at 13.8% and Corporation Tax at 20%. For the cover they need, the monthly premiums would be £50 for Bethany and £30 for Ross.

The table below shows how cost-effective it is to provide life insurance through a relevant life policy, treating the premiums for such insurance as an allowable business expense for the company.

		Personal life insurance		Relevant life insurance	
		Bethany	**Ross**	**Bethany**	**Ross**
Cost to **employee**	Monthly premium (from net salary)	£50	£30	n/a	n/a
	National Insurance contribution (@2%)	£1.72	£1.03	n/a	n/a
	Income Tax (@40%)	£34.48	£20.69	n/a*	n/a*
	Total cost to employee **	**£86.20**	**£51.72**	**n/a**	**n/a**
Cost to **employer**	Monthly premium	n/a	n/a	£50	£30
	National Insurance contribution (@13.8%)	£11.90	£7.14	n/a	n/a
	Total gross cost	£98.10	£58.86	£50	£30
	Less Corporation Tax (@20%)	£19.62	£11.77	£10	£6
	Tax adjusted total cost	**£78.48**	**£47.09**	**£40**	**£24**

* The payments employers make are not subject to Income Tax because they are not normally assessable on the employee as a benefit in kind.

** These are the gross earnings required to leave sufficient net income to pay the premium.

The information provided in each example is for illustrative purposes only and the examples are purely fictitious. The illustrations are based on our understanding of current law and HM Revenue & Customs practice as at December 2015 which may change in the future

Tax calculations are based on 2015/16 tax rates and may also change in the future. The calculations assume that the same rate of Income Tax/National Insurance applies to the whole of the premium or sums used to fund the premium. Before proceeding with the cover, we recommend you seek professional advice from a financial adviser and a qualified tax adviser to ensure there aren't any adverse taxation consequences for the employee, employer and trustees.

Any tax and National Insurance is calculated based on the cost to the employee, i.e. how much would it cost an employee in total to pay a premium, taking account of Income Tax, National Insurance and the premium.

Looking at the example for Helen, to be able to pay a premium of £1,000 per annum (£ 83.33 per month), she would need to earn £143.67 on which she would have to pay income tax of £57.47 (£143.67 x 40%) and national insurance of £2.87(£143.67 x 2%) to reach the net amount of £83.33 (£143.7- £57.47- £2.87) which can be used to pay the premium.

To get to the total net cost to the employer and leave the employee with sufficient net income to meet the premium, you would need to add the employer's National Insurance contribution costs and then deduct Corporation Tax Relief.

Writing a policy into trust

A relevant life insurance policy must be written into trust, with the employee's family and dependants as beneficiaries. As with any non-pension discretionary trust, the trust itself can be subject to Inheritance Tax periodic and exit charges. Periodic charges are made if a trust has valuable assets on a 10-year anniversary.

While the employee is alive and well, the value of the trust asset (the policy) will be negligible. So any charges are unlikely to happen, unless the employee dies and the claim is paid into the trust just before a 10th anniversary and there is not enough time to pay the assets out to the beneficiaries. In this case, a periodic charge will arise on the value of those assets in excess of the current nil rate band at a rate of up to 6%.

If the assets remain in the trust past a 10-year anniversary, there could be a potential exit charge when the trust is paid out. This will be a proportion of the last periodic charge due, again up to a maximum of 6%.

However, where assets are paid out as soon as possible following a claim, there's unlikely to be any significant exit charge. There also won't be any exit charge if the assets are paid out within three months of a 10-year anniversary.

How do I set up relevant life insurance with AIG?

The business or employer will need to agree to pay the premiums. You will also need to speak to your financial adviser, who can apply for the insurance online, using our quote and apply system. The insurance must be written in trust, with the business as the cover owner and you or the employee as the person covered.

The person covered will need to provide information about their health and medical history, earnings and occupation.

How much cover can I have?

Most death-in-service benefits allow businesses to cover their employees for up to 4 x their salary. AIG Relevant Life Insurance is more flexible, allowing you to choose a payout worth anything up to a maximum of:

Ages 17-39 – 30 x salary
Ages 40-49 – 25 x salary
Ages 50-59 – 20 x salary
Ages 60-71 – 15 x salary

Valuable support services

Employee benefits have an important role to play within a business. While legislation means we can't add extra financial benefits to relevant life insurance, we do include some valuable extra support including child bereavement counselling from Winston's Wish and free medical advice from Best Doctors.

It means the employee and their family get more than just financial support if they ever have to claim, and that they have extra medical support services available to them throughout the life of the policy too.

About Winston's Wish

Families, particularly when struck by their own grief, may find it difficult to give children the right support. Schools and other public services can also struggle to recognise, understand or manage a grieving child's behaviour.

When parents or carers don't know what to say or what to do, Winston's Wish is available to help families make sure they're giving their children the right support.

About Best Doctors®

Founded in 1989 by Harvard Medical School professors, Best Doctors has established a worldwide database of 50,000 doctors in over 400 different disciplines, each of whom has been chosen by other specialists in their field as one of the best in the world.

- It can be used by the person covered, their partner and any dependent children;
- It can be used as soon as the policy goes on-risk;
- There is no limit to the number of times it can be used;
- Pre-existing conditions are not excluded;
- Enquiries do not have to relate to a claim or a condition covered by the policy.

If our policyholders are ever worried about the diagnosis or treatment options they, their partner or any dependent children are given, they can use Best Doctors to get second medical opinions and information about treatment from a leading specialist in their condition.

For more information visit **www.aiglife.co.uk**, speak to your financial adviser or find one at **www.unbiased.co.uk**

www.aiglife.co.uk

AIG Life Limited. Telephone 0345 600 6820. Registered in England and Wales. Number 6367921. Registered address: The AIG Building, 58 Fenchurch Street, London EC3M 4AB.

EDCO1773-0516