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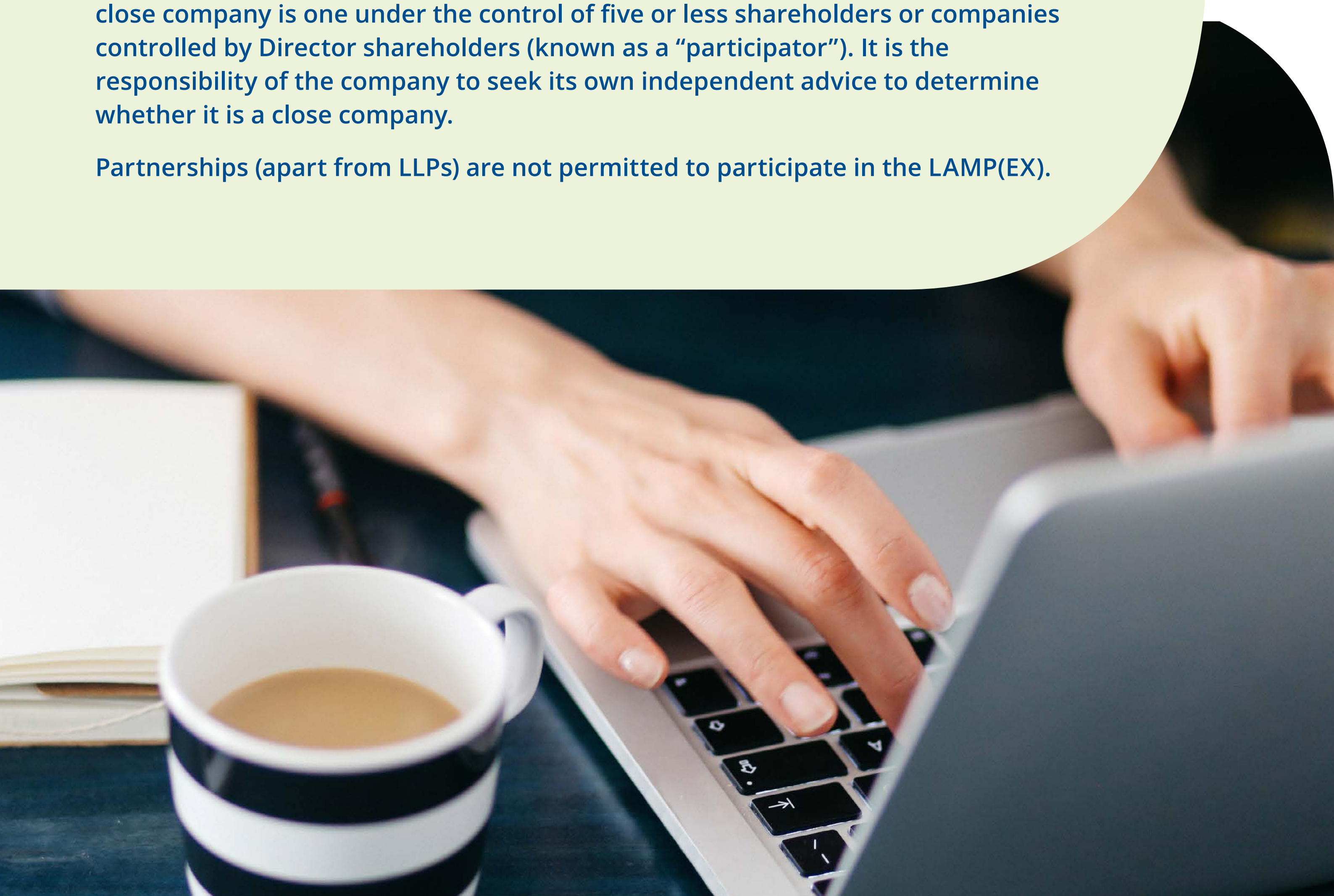
Excepted Group Life
Technical Bulletin

This document provides an overview of EGLPs, including important information on entry, periodic and exit charges. It also contains an FAQs section on common EGLP queries.

Please note that the rules that apply have some differences depending on whether the participating employer is a non-close company, a close company or a Limited Liability Partnership.

Whether a corporate entity is a close company is complex. Broadly speaking a close company is one under the control of five or less shareholders or companies controlled by Director shareholders (known as a "participator"). It is the responsibility of the company to seek its own independent advice to determine whether it is a close company.

Partnerships (apart from LLPs) are not permitted to participate in the LAMP(EX).



EGLP details	EGLP rules
• Are set up under a discretionary trust and the only asset in the trust will be the EGLP • Are subject to the Inheritance Tax (IHT) rules that apply to discretionary trusts (they are treated as relevant property) • Are not pension arrangements and do not count towards an individual's Lump Sum and Death Benefit Allowance (LSDBA) • Must meet the following seven conditions set out in sections 481 and 482 of the Income Tax (Trading and Other Income) Act 2005	• The policy must only provide a capital sum payable on death before age 75 • The same method for calculation of the capital sum and any limitation, such as stated fixed benefit or multiple of earnings, must be applied to all members under the policy • The policy must not provide a surrender value other than a refund of 'unused' premiums • Only the benefits set out above may be provided by the policy • Benefits payable under the policy must be paid to either an individual entitled to them (or a charity) or a trustee for payment to such individuals • No person whose life is insured under the policy may receive any death benefit in respect of another group member purely on the basis that they are one of the insured persons under the policy • The policy is not taken out with the main purpose of avoiding the payment of tax

Entry charge

Is there an entry charge when the trust is established?

Non-close companies:

EGLPs are normally taken out by the employer and assigned into the trust. In this situation:

- HMRC would regard the employer as the settlor
- There will usually be no IHT tax liability on the settlement of the EGLP into the trust as corporate bodies are typically exempt from making a chargeable transfer (i.e. only an individual can make a chargeable transfer).

Close companies:

A close company is not exempt from entry charges. A close company may be subject to an entry charge where an employee is terminally ill at the point of the settlement of the EGLP into the trust and the value of the transfer (i.e. the benefit payable in respect of the terminally ill employee) is in excess of the close company's participators' available nil rate bands (currently £325,000). In this scenario, it is deemed that there is a value in the trust at the time of the settlement, which is treated from an Inheritance Tax perspective as a Chargeable Lifetime Transfer and gives rise to a tax charge of 20% on the full excess amount above the available nil rate bands. If the nil rate bands have been used up elsewhere the liability will be 20% of the full value (not capped at £325,000).

It is the close company which is liable for the entry charge (with the participators of the close company being liable if the tax charge remains unpaid).

There is also a risk that for close companies any proceeds paid out of the policy may be subject to additional tax charges. Unum Limited is not responsible for advising on the specific position for your company and strongly recommends close companies wishing to participate in the Unum EGLP Master Trust take independent advice on their tax position.

Periodic charge

What is the periodic charge and when will it apply?

A periodic charge is an IHT charge which can arise at each 10 year anniversary of the settlement of the EGLP into the trust.

The charge will only apply if there is a value in the trust at the 10 year anniversary. In practice there will only be a value at that point if:

- A claim has been paid to the trustees but they have not distributed the benefit; or
- A member has died but a claim has not been submitted or paid; or
- A member was terminally ill and died within the 12 months after the 10 year anniversary

How is a periodic charge calculated at each 10 year anniversary?

The periodic charge applies on the value of the trust over the nil rate band available to the trust at the 10 year anniversary. The maximum nil rate band available is £325,000.

The maximum rate of periodic charge is 6% (i.e. 30% of the lifetime rate of 20%). The following example highlights how the periodic charge applies:

Example - EGLP covering all members for a benefit of £200,000

6 years after the trust was established the first claim arises:

- £200,000 is paid to the trustees and immediately distributed

9 years and 9 months after the trust was established the second claim arises.

- £200,000 is paid to the trustees but they do not distribute the proceeds until 10 years and 6 months after the trust was established
- There is a value in the trust at the 10 year anniversary (£200,000 from the second claim) and a periodic charge arises
- The nil rate band available at the 10 year anniversary is £325,000 less £200,000 paid out on the first claim = £125,000

The value in the trust above the nil rate band = £75,000

- The rate of periodic charge is calculated as:
  - £75,000 x 20% (the lifetime rate) = £15,000
  - £15,000 is then expressed as a percentage of the £200,000 value in the trust at the 10 year anniversary = 7.5%
  - 30% x 7.5% = 2.25% (this is known as the settlement rate)
- The periodic charge is calculated as:
  - £200,000 x 2.25% = £4,500

Exit charge

What is the exit charge and when will it apply?

An exit charge is an IHT charge which arises when capital leaves the trust (i.e. when the trustees distribute the benefits).

In practice

- Exit charges in the first 10 years will be nil if there was no IHT liability when the EGLP was settled into the trust
- After the first 10 years the exit charge will:
  - Depend on whether a periodic charge arose at the previous 10 year anniversary
  - Be nil if there was no periodic charge at the previous 10 year anniversary
  - Be nil if there was a periodic charge at the last 10 year anniversary but the money is paid out within three months of the 10 year anniversary

How is the exit charge calculated?

The exit charge will depend on:

- The rate of periodic charge at the previous 10 year anniversary (the settlement rate)
- The length of time the relevant property has been held in the trust since the last 10 year anniversary. This is measured in quarters during each 10 year period – each quarter being 1/40th

We can now show how the exit charge would apply in our previous example:

Example - EGLP covering all members for a benefit of £200,000

An exit charge arises when the benefit from the first claim is distributed 6 years after the trust was established. The rate is nil because there was no IHT when the trust was established.

An exit charge arises when the £200,000 from the second claim is distributed 10 years and 6 months after the trust was established:

- The settlement rate at the last 10 year anniversary was 2.25%
- The property has been in the trust for 2/40th since the last 10 year anniversary
- The exit charge is calculated as:
  - £200,000 x 2.25% x 2/40 = £225

15 years after the trust was established a third claim arises.

- £200,000 is paid to the trustees and immediately distributed
- The exit charge is calculated as:
  - £200,000 x 2.25% x 20/40 = £2,250

FAQs

What is meant by "terminally ill"?

Unum follows the definition of terminally ill as set out in the Finance Act 2004. An employee is considered to be terminally ill where the trustee of the Unum EGLP Master Trust has received evidence from a registered medical practitioner that the member is expected to live for less than one year.

What are the implications if a policy is switched from one insurer to another during the 10 years?

There will be no implications as the trust remains the same and there has been no exit from the trust. This is simply a change in the underlying asset.

Please refer to our Excepted Group Life Master Trust FAQs document UP3394 for information on policies held in the Unum EGLP Master Trust.

What are the implications if a registered policy is cancelled and a new EGLP taken out?

The registered policy will lapse without value and the trust will become an empty shell.

A new trust will be established to hold the EGLP and the new trust and 10 year period start from that point.

Will HMRC consider tax avoidance to be the main purpose of an EGLP?

The main purpose of setting up an EGLP is to provide life assurance for the benefit of employees.

It is generally accepted that taking out an EGLP is using a method permitted by legislation to pay life assurance benefits in a tax-efficient way. Taking out an ISA rather than a savings account with taxed interest may be a useful comparison.

We have not seen or been made aware of any HMRC challenge to EGLPs on the basis of tax avoidance.

Does cancelling and replacing the trust avoid the 10 year anniversary charge?

If the trust and policy are cancelled and reconstructed on a regular basis there is a risk that HMRC may take the view that this constitutes an avoidance manoeuvre - as the only reason the approach is being taken is to avoid the periodic and/or exit charges and one policy is being replaced with an identical policy.

It could be argued that this would be more of an issue if the new EGLP was on preferential terms (e.g. if a member was terminally ill but cover continues when cover would not be available on the open market).

There is a risk that if an EGLP is transferred from Trust A to Trust B HMRC will treat the date of settlement as the original settlement into Trust A for IHT purposes.

There seems to be little or no advantage to cancelling and replacing the trust before the 10 year anniversary.

Do trustees need to report any terminally ill members?

We understand that HMRC would not expect trustees to ask each member if they have a diagnosis of a terminal illness for the 10 year valuation (or for close companies on settlement of the EGLP into the trust). So a return would only be needed if the trustees were aware that there was value in the settlement at that time.

If the trustees are notified of a death in the 12 months after the 10 year anniversary, they should check whether a terminal diagnosis had been made on or before the 10 year anniversary and an IHT return be submitted if necessary.

Payment of Premiums – LLPs

Payment of premiums for the EGLP made by an LLP on behalf of its members are not considered to be wholly and exclusively for the purposes of the trade and as such will not be deductible for income tax purposes. These payments will therefore be subject for income tax.

Support

How we can support EGLPs?

We can:

- Set up EGLPs linked to a registered group life policy or on a standalone basis
- Include multiple EGLPs on one quotation
- Switch a registered policy to an EGLP with a simple "change of basis" application form. New policy terms will apply from the date of the change.
- Offer access to the Unum EGLP Master Trust which provides a simple and hassle-free solution for employers who want to put Group Life Cover in place for their employees

For more information please contact your Unum Sales Consultant

The information contained in this document is based on Unum's current interpretation of the relevant legislation which may itself change and develop with the passage of time. The information does not constitute legal or professional advice and should not be relied upon as such. You should always obtain independent legal advice about your specific circumstances. Unum does not accept any responsibility or liability for the accuracy or completeness of the information. Furthermore Unum does not accept any responsibility for any loss or damage of whatever nature which may arise where there has been reliance upon the information set out above.