Group Protection

Helping you understand Excepted Group Life Policies (EGLP)

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Introduction

This document gives you information about Excepted Group Life Policies (EGLP) and answers the following questions:

- What is an EGLP?
- What must I remember when I set up an EGLP?
- Why choose an EGLP?
- Should I set up an EGLP or a registered scheme for all my employees?
- How is an EGLP taxed?

The information we've given is based on our understanding of current law and tax rules. We suggest you talk to your legal adviser before setting up, or changing employment benefits.

We've used plain language to help make this guide easier to understand. You'll find explanations of any technical terms we use in the glossary at the end of this document. Where terms in the glossary appear in the main text we've highlighted them **like this**.

To understand the purpose of an EGLP and whether it's the suitable option, you'll find it useful to know a bit about other types of group life assurance schemes. Therefore, to help you compare, this guide also contains some information about **registered schemes** and **employer-financed retirement benefits schemes (EFRBS)**.

The different types of group life assurance

You can set up a group **policy** that pays a lump sum benefit for dependants and relatives after the death of an employee, partner or Limited Liability Partnership (LLP) member in three different ways:

1. A **policy** covering **registered scheme benefits**
2. An EGLP
3. An **employer-financed retirement benefits scheme (EFRBS)**.

Each way is defined by law and treated differently for tax. The tax treatment is usually the main reason why you will choose one type of assurance over another.

Depending on your requirements, you may choose a **registered scheme policy** to cover your employees.

An EGLP can be chosen to cover employees who already have a high level of **registered scheme benefits**. You may also ask us to set up an EGLP for employees who have **enhanced protection** or a form of **fixed protection**. EGLP's are often chosen to cover self-employed equity partners and LLP members.

If you don't choose a **registered scheme** or an EGLP to cover your employees, an **employer-financed retirement benefits scheme** is the default option. These are rare because of the high levels of tax that may become due.

There are other types of group life assurance cover for self-employed equity partners and LLP members; however, they aren't relevant for this document.

What is an EGLP?

An EGLP is a **policy** that meets all seven of the following conditions:

1. It can only pay lump sum benefits for deaths before age 75.
2. Benefit must be worked out in the same way for everyone included in the EGLP.
3. If the EGLP is cancelled, it must not have a cash value. However, unused premiums can be refunded.
4. Only the benefits set out in the EGLP can be paid.
5. Benefits can only be paid to:
   (i) Individuals
   (ii) Charities
   (iii) Trusts set up for individuals.
6. Benefit cannot be paid to another person also covered by the EGLP. However, benefit can be paid if that other insured person is a dependant or relative of the person who died.
7. The EGLP must not be set up with the main purpose of avoiding tax.

There's more information about some of these conditions under the section 'What must I remember when I set up an EGLP?' on page 5.

An EGLP covering one person is often called a **relevant life policy**.

What must I remember when I set up an EGLP?

You need to remember some of the conditions an EGLP must meet.

1. It can only pay lump sum benefits for deaths before age 75.

   We agree a day cover will stop. This can be the later of the person reaching age 65 or their state pension age. Alternatively it can be reaching a set age. However, we cannot cover a person under an EGLP once they have reached age 75.

2. Benefit must be worked out in the same way for everyone included in the EGLP.

   The benefit formula we insure under an EGLP must be the same for everyone we cover under it.

   We can cover benefit as a multiple of earnings, or a flat amount, for example £100,000. If benefit is based on earnings, the earnings definition and the frequency we allow for changes in earnings, must be the same for everyone included in the EGLP.

   The benefit can be limited to a maximum or a minimum. Any maximums and minimums must be the same for everyone included in the EGLP.

   The benefit can include a deduction, or an addition, for example a fixed cash amount. If it does, the same deduction or addition must apply to everyone's benefit. We cannot offset the value of a person's pension fund, as this will vary from person to person.

   If we include a restriction or exclusion in our **policy** terms, we must apply it to everyone included in the EGLP.

   If you need more than one benefit formula to meet the EGLP conditions, you'll need to set up a separate EGLP for each benefit formula. We will often group EGLP together for administration and accounting purposes. Normally only one **trust** and proposal form will be needed.

3. Benefits can only be paid to:

   (i) Individuals

   (ii) Charities

   (iii) Trusts set up for individuals.

   A **trust** is a legal document that describes who can receive benefit from a **scheme**. A **trust** used to pay benefit from an EGLP must not allow anyone other than an individual or a charity to benefit from the EGLP. It's also possible for the EGLP **trust** to allow benefit to be paid on to a different **trust** set up for an individual.

   We're sometimes asked why our specimen **trust** doesn't allow benefit to be paid to the estate of the person who has died. HM Revenue & Customs' website suggests this is possible, however:

   (i) Legislation says otherwise, only allowing benefit to paid to individuals, charities or **trusts** set up for individuals. A person's estate could go to another body that doesn't meet this condition.

   (ii) If the **policy** covers equity partners or LLP members and benefit can be paid to the estate, the insured persons will have to pay pre-owned asset tax every tax year.

4. Benefit cannot be paid to another person covered by the policy.

   However, benefit can be paid if that other insured person is also a dependant or relative of the person who died.

Benefits from an EGLP are normally paid under **trust**, and you'll need to consider points 3 and 4 shown above when you set up your **trust** and any **scheme** rules. Our EGLP terms will require the **trust** or **scheme** rules you use to limit the potential beneficiaries to only those who may receive benefit from an EGLP.

Why choose an EGLP?

Most businesses will choose to set up life assurance cover using a **registered scheme**; however, a **registered scheme** isn't always suitable. For businesses that need an alternative, an EGLP is often the answer. We've given some examples below where an EGLP may be chosen.

1. One or more employees have high **registered scheme benefits**.

   The **lifetime allowance** charge (currently 55%) is a tax against a person's **registered scheme benefits** paid above the **lifetime allowance**. Employees with large **registered scheme** pension values may prefer to receive their life assurance benefits outside a **registered scheme**.

   The **lifetime allowance** and the **lifetime allowance** charge do not apply to an EGLP, and a business may consider providing life assurance cover for its employees in this way.

   A business will need to satisfy itself that the main purpose of the EGLP isn't to avoid tax. They may want to talk their legal adviser.

2. One or more of the employees have applied for **enhanced protection** or a form of **fixed protection**.

   The Government introduced **enhanced protection** and the forms of **fixed protection** when tax laws changed and tax allowances reduced. Employees could apply for these protections to protect their existing **registered scheme** pension rights from tax charges. If they did, additional restrictions apply to their **registered scheme** membership. If they don't keep to these restrictions, they will lose the protection and more tax may be due when a **registered scheme benefit** is paid.

   Sometimes an employer cannot include an employee in a **registered scheme** because they will lose their **enhanced protection** or **fixed protection**. EGLP cover will not affect an employee's **enhanced protection** or **fixed protection**.

   We can insure dependants' pension cover under an EGLP. This is an unusual feature because an EGLP condition says benefit must be paid as a one-off lump sum. To meet this condition, we convert the dependants' pension to a lump sum using an actuarial calculation at the time of the insured person's death. This calculation takes into account the age and details of the person who will receive the benefit, and the annuity rates at that time.

3. Self-employed equity partners and LLP members cannot set up a **registered scheme** for themselves.

   Self-employed equity partners and LLP members cannot set up a **registered scheme** just for themselves, however they can join a **registered scheme** set up to provide death-in-service benefits for their employees. This often isn't the preferred route for self-employed equity partners and LLP members because:

   (i) The **scheme** rules will be available to all people included in it. The firm may not want the employees to find out the benefit level for equity partners and LLP members.

   (ii) Self-employed equity partners and LLP members are often well paid. They usually have large pension investments and need large life assurance cover.

   Self-employed equity partners and LLP members can ask us to set up a partners' life assurance **policy** as an EGLP.

4. The taxation of death-in-service benefits that aren't registered or insured as an EGLP.

   Chargeable gains tax rules will apply. This means the policyholder may have to pay tax after the second death under the **policy**, and each death afterwards. The **chargeable gains tax** rules do not apply to an EGLP.

   If the non-registered **scheme** covers employees, it will be treated as an **employer-financed retirement benefits scheme (EFRBS)**. In addition to the **chargeable gains tax** rules, an employer may not get tax relief on the premiums they pay; the premiums are treated as a **benefit in kind** (P11D benefit) for the employees and all benefit payments will be taxed as income. Employers rarely set up an **employer-financed retirement benefits scheme (EFRBS)** because their tax treatment is generally unattractive.

Should I set up an EGLP or a registered scheme for all my employees?

We believe EGLP should only be used for those employees who have applied for **enhanced protection** or a form of **fixed protection**. It could also be used for employees who already have large **registered scheme benefits**.

You may also choose to set up an EGLP for all employees, if most are affected by these issues.

For most other situations you will normally choose a **registered scheme**. A **registered scheme** providing only group life assurance benefits is relatively easy to set up and has few HM Revenue & Customs reporting requirements. A **registered scheme** also has advantages over an EGLP. This is why many employers choose a **registered scheme** over an EGLP. The **registered scheme** advantages include:

1. Tax relief is available on the premiums an employer pays for a **registered scheme**. While in practice HM Revenue & Customs agrees tax relief is available for an EGLP, the legislation isn't so clear. For any employee financed portion of premiums, tax relief through salary sacrifice is available for **registered schemes**, however not for an EGLP.
2. **Registered schemes** can pay lump sum life assurance benefit tax-free up to the **lifetime allowance**.
3. **Registered schemes** can pay dependants' pension benefits, however an EGLP cannot. Only a lump sum equivalent can be insured under an EGLP instead.
4. An EGLP will only allow benefit to be paid to individuals or charities. **Registered schemes** can pay benefit to a wider group.
5. A single **registered scheme** can provide more than one benefit basis. An EGLP can only include one benefit basis under each **policy**. A separate EGLP for each different benefit basis increases administration.
6. The legislation for **registered schemes** is well documented. HM Revenue & Customs provide **registered scheme** support for both employers and **trustees**. The legislation for EGLP isn't so clear and employers may need to pay for legal advice to clarify particular points.
7. **Exit charges** and **periodic charges** may apply to an EGLP; however, these charges currently don't apply to a **registered scheme**.

We'd recommend that you check with your employees to verify if they have **enhanced protection** or a form of **fixed protection**. This will help you decide which arrangement will be suitable.

How is an EGLP taxed?

The **lifetime allowance** and the **lifetime allowance** charge (currently 55% of the benefit) will not apply to any benefit paid from an EGLP. Additionally, the **chargeable gains tax** rules do not apply to an EGLP.

However, an EGLP is not without tax charges. There are also small differences between the taxation of an EGLP set up for employees, and an EGLP set up for self-employed equity partners or LLP members.

For an EGLP that covers employees and pays benefit under a discretionary **trust**:

1. The insurance premiums you pay may qualify for tax relief as a business expense. For this tax relief, the local tax inspector must agree the **policy** is wholly and exclusively for business purposes.
2. The insurance premiums are not treated as a **benefit in kind** (a P11D benefit) for the employees.
3. Lump sums are subject to the normal tax rules that apply to discretionary **trusts**. This means **periodic charges** and **exit charges** may apply. These charges are worked out when benefit is paid. Each of the two charges will not exceed 6% of the benefit.

For an EGLP that covers self-employed equity partners or LLP members, and pays benefit under a discretionary **trust**:

1. Self-employed equity partners and LLP members cannot get tax relief on the premiums they pay for their cover.
2. Lump sums are subject to the normal tax rules that apply to discretionary **trusts**. This means **periodic charges** and **exit charges** may apply. These charges are worked out when benefit is paid. Each of the two charges will not exceed 6% of the benefit.

Glossary

Benefit in kind

A benefit in kind is a taxable benefit an employee may receive from their employer. A benefit in kind will not be any form of pay. Examples of a benefit in kind include a company car, private medical insurance and critical illness cover.

The employer will know the value of the benefit in kind, and that value will normally be taxed as income.

Benefits in kind are sometimes called P11D benefits.

Chargeable gains tax

Chargeable gains tax is a tax against profits made on a one-off basis. For example, a business may have to pay chargeable gains tax on any profit it makes when it sells an asset.

Chargeable gains tax will not apply to a **registered scheme** or an EGLP.

For other group life assurance **policies**, chargeable gains tax will not apply to the first benefit payment, however, it may apply to second or subsequent benefit payments. This is because of the way the chargeable gain is worked out:

(surrender value + value of all previous claims) – all premiums paid
= chargeable gain

The relevant tax rate is then applied to the chargeable gain.

For the first claim the value of all previous claims will be zero, therefore there cannot be a chargeable gain.

If there is a chargeable gain, we need to send a chargeable gain certificate to the policyholder, and sometimes, HM Revenue & Customs as well.

Employer-financed retirement benefits scheme (EFRBS)

A **scheme** set up for employees that is not a **registered scheme** or an EGLP. Their tax treatment is generally unattractive.

Group life assurance for self-employed equity partners or LLP members can never be an employer-financed retirement benefits scheme because there isn't an employer-employee relationship.

Enhanced protection

Enhanced protection was available to people with **registered scheme benefits** on 5 April 2006. It allowed them to protect their **registered scheme benefits** from the **lifetime allowance** and the **lifetime allowance** charge when it was introduced on 6 April 2006.

If a person applied for enhanced protection, certain restrictions apply to their membership of a **registered scheme**. These restrictions sometimes prevent the employee being covered for life assurance under a **registered scheme**. If a person doesn't keep to these restrictions, they will lose their enhanced protection.

Exit charges

Exit charges are a type of inheritance tax that may apply to group life assurance benefits paid through a discretionary **trust**. Exit charges do not apply to **registered schemes**.

Exit charges can be complicated to work out. They are based on the time elapsed since the later of the **trust** start date, or the last ten-year anniversary of the **trust**. The exit charge rate moves from 0% up to 6% over each ten-year period. The rate may also be reduced if previous benefit payments have been taxed, or a tax allowance hasn't been used up.

Fixed protection

Fixed protection was available to people with **registered scheme benefits** on 5 April 2012. It allowed them to protect their **registered scheme benefits** from the reduction in the **lifetime allowance** on 6 April 2012. Fixed protection 2014 was available to anyone with **registered scheme benefits** on 5 April 2014. It allowed them to protect their **registered scheme benefits** from the reduction in the **lifetime allowance** on 6 April 2014. Fixed protection 2016 was available to anyone with **registered scheme benefits** on 5 April 2016. It allowed them to protect their **registered scheme benefits** from the reduction in the **lifetime allowance** on 6 April 2016.

If a person applied for fixed protection, certain restrictions apply to their membership of a **registered scheme**. These restrictions sometimes prevent the employee being covered for life assurance under a **registered scheme**. If a person doesn't keep to these restrictions, they will lose their fixed protection.

Lifetime allowance

The maximum amount of tax-free benefits that can be paid for an individual from all **registered schemes**. HM Treasury sets and reviews the lifetime allowance. From 6 April 2018 it was set at £1,030,000; this is reviewed on a regular basis.

Periodic charges
Periodic charges are a type of inheritance tax that may apply to group life assurance benefits paid through a discretionary **trust**. Periodic charges do not apply to **registered schemes**.

Periodic charges can be complicated to work out. They are based on the value of the **trust** at a 10-year anniversary. Most legal advisers believe a **trust**, set up only for group life assurance benefits, can only have a value for a period between the insurer paying the benefit to the **trustees**, and the **trustees** paying it on to the people entitled to it. Unless there is a death just before a ten-year anniversary, or a terminally ill insured person at that anniversary, most **trusts** will not have a value at that time.

The periodic charge rate can be from 0% up to 6%.

Policy
The insurance contract is agreed between us and the **trustees**. The **trustees** use the policy to cover all, or some, of their liability to pay life assurance benefit under the **scheme**. We do not have a direct contractual relationship with employees.

Registered scheme
A **scheme** registered with HM Revenue & Customs. Registered schemes can provide tax-free benefits up to the **lifetime allowance**. A registered scheme just providing life assurance benefits is often called a registered stand-alone death-in-service scheme. Registered schemes can also provide pensions on retirement.

Registered scheme benefits
The benefits provided under a **registered scheme**.

Relevant life policy
A **policy** covering one person that meets the conditions of an EGLP.

Scheme
The legal contract the principal employer sets up to provide life assurance benefits to its employees. The scheme consists of a **trust** and scheme rules. The **trust** and rules describe who is included, the benefits provided and who the **trustees** can pay the benefit to.

The principal employer and **trustees** have responsibilities and liabilities recorded in the **trust** and rules. As an insurer, our liabilities are recorded separately in the **policy**.

We have specimen **trust** and rules documents an employer may use to set up their scheme. Before setting up a scheme, we suggest the employer talks to their legal adviser to make sure our specimen documents meet all their needs.

Self-employed equity partners and LLP members decide together the eligibility and benefits of their **policy**. Therefore they don't set up a scheme. They will still use a **trust** to make sure benefit is paid to the right people, and to take advantage of tax rules.

Trust
The legal document the principal employer uses to set up the **scheme** for its employees. The trust will be used to record important high-level information including the **scheme** name, the day the **scheme** starts and appoints **trustees**.

Self-employed equity partners and LLP members use a slightly different trust that doesn't set up a **scheme**. It states its purpose (to pay the benefits from the **policy**), who the **trustees** are, and the day it was set up from.

A discretionary trust is a type of trust a business will normally use to pay group life assurance benefits because of its tax advantages. A discretionary trust describes all the people who may receive benefit after an insured person dies. These people include dependants, relatives, charities and anyone else the insured person has chosen benefit to go to. The **trustees** decide who gets the benefit. They must act in the best interest of everyone and do not have to pay benefit to the people chosen by the insured person. **Trustees** can be taken to court if they make a bad decision.

Trustees
The trustees are responsible for running the **scheme** and paying benefit in line with the **trust** and **scheme** rules.

For stand-alone death-in-service **schemes**, the trustee will often be the principal employer. However, the principal employer can appoint a board of trustees or a trustee company instead.

For **schemes** providing pension benefits on retirement, the principal employer must appoint separate trustees.

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Q0039984 08/18