Questions and answers on Relevant Life Policies (RLPs)

Synopsis: A series of questions on Relevant Life Policies.

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How is an RLP established?

RLPs can only be effected by employers for their employees. The employer must therefore apply for the policy. The employer can be a limited company, partnership, LLP or a sole trader.

Is anything else required to establish an RLP?

In addition to completing the application form the employer must also complete the Relevant Life Policy trust documentation.

Who can be insured under an RLP?

There must be an employer/employee relationship. Directors of a company, including shareholding directors, and officers of a company are also treated as employees for this purpose. However, partners, LLP members and sole traders are not employees.

How are the benefits under an RLP payable?

The main benefit provided under an RLP is a benefit on death before age75. Other benefits available are in respect of ill health, disablement and death by accident but these benefits are only payable as long as the life assured is still in employment.

The benefit will be paid by the insurer to the trustees of the RLP trust. The trustees have discretion as to who should receive the benefit from the classes of beneficiaries specified in the trust.

Does the life assured/employee have any influence over who should benefit on their death?

The employee can and should complete a nomination form addressed to the trustees of the RLP trust. This is a non-binding expression of wishes to their trustees. This is similar to the method of nominating beneficiaries under a registered pension scheme.

Who should be the trustees of the RLP trust?

The employer will usually be a trustee. Most RLP trusts allow for the appointment of other trustees who could include an independent person or a member of the employee’s family.

If a benefit under an RLP is paid for ill health or disablement, is the life assured entitled to this benefit?

Any benefit payable will be paid in the same way as the death benefit, i.e. to the trustees of the trust. As the employee is normally one of the trust beneficiaries, the trustees can make the payment to the employee or the employee's family. The trustees will need to consider all the circumstances at the relevant time in order to decide who should receive the benefit.

If the life assured changes employment what are the consequences in relation to the RLP?

Much depends on the circumstances and the terms of the policy in question. If the life assured takes up a new employment, it may be that the new employer will be prepared to take over premium payments and so keep the cover in force, provided the policy in question allows for this. The new employer would normally become a trustee of the RLP trust. Ideally the trust provisions should contemplate such a possibility.

Can the policy continue if employment ceases and the life assured does not take up new employment?

There is no statutory bar on this so the policy can continue if the terms of the policy allow for this. However, terminal illness, disability, ill health and death by accident benefits must cease when employment ceases. If ongoing premiums are to be paid by the life assured, it will be necessary to remove the life assured as a beneficiary under the trust either by the life assured completing a disclaimer form or, if the trust allows for this, by the trustees excluding the life assured from benefit. This is needed to avoid an inheritance tax (IHT) gift with reservation of benefit problem on later premium payments.

Apart from the income tax benefits, are there any other tax implications in connection with an RLP?

There are no other tax implications as long as the life assured is alive. Once the death benefit is paid to the trustees, as the trustees will hold the benefit on discretionary trust then the normal IHT rules which apply to the taxation of discretionary trusts (the "Relevant Property regime") will also apply here. This will mean potential periodic charges and exit charges.

Is there a maximum benefit that can be paid under an RLP?

There is no statutory maximum. Insurers may have their own commercial maxima and associated underwriting/financial underwriting limits, and the sum assured should be reasonable in relation to securing deductibility for premiums paid by the employer under the "wholly and exclusively" rules on the provision of benefits under the policy.

Can an RLP be assigned by the trustees to the leaving employee or another beneficiary?

As the employee is usually a potential beneficiary under the trust, it should be possible for the RLP trustees to assign the policy to the employee (as a beneficiary) after it has been irrevocably appointed to that beneficiary by the trustees. The RLP legislation does not specifically cover such assignments and HMRC practice in this area is unknown. Therefore, it is not possible to be categoric as to the tax results of such action.

There are two potential taxation outcomes if the policy is assigned to an employee or beneficiary who is also a member of the family of the leaving employee...

- It could be argued that as the assignment was to the beneficiary in consequence of the absolute appointment to them under the trust, it is not an assignment for consideration. As the premiums were previously paid by the employer, this would not lead to any liability to income tax or capital gains tax. There could, however, be an exit charge for IHT purposes, but, if the life assured is still in reasonable health, a charge is very unlikely.

- On the other hand, HMRC could take the view that because the settlor and trustee is the employer, and the assignee is the employee or a member of the employee's family, then previous premiums paid by the employer could potentially be subject to income tax for the leaving employee based on the "cost to the employer" principle. Indeed, this could apply even though the beneficiary does not personally benefit from the assignment. Furthermore, as the policy is now a "second-hand policy", the employee having given consideration for it, capital gains tax may be charged on any claim proceeds.

This interpretation does, to a degree, go against the intention of the RLP legislation. However, as stated above, legislation does not specifically deal with assignments.

Can an RLP be used in business protection planning?

Given that the underlying intention of an RLP is to provide benefits for the family of a deceased employee, if two or more shareholders in a close company set up RLPs and include other shareholders as a class of beneficiary the policies could, in theory, be used for business protection planning, i.e. to fund the purchase of the co-owner's shares. It is not thought that RLPs should be used in this way as it means the cover is being used in a way not contemplated by the legislation. Furthermore, as the RLP trust is a discretionary trust, there could not be a guarantee that the co-shareholders would actually receive any funds from the trust.

It has also been suggested that if RLPs are set up by director/shareholders for the benefit of their family, the shares in the company could be left directly under a will to the surviving shareholders. This planning would clearly be vulnerable to one of the owners changing their will.

Summary of RLP benefits

- Tax relief on the premiums for the employer subject to satisfying the "wholly and exclusively" test.

- No assessment of premiums on the employee as benefit in kind, provided the premiums are not paid under a salary sacrifice arrangement.

- Premiums not taken into account in determining the available Annual Allowance for registered pensions.

- No assessment for the purpose of National Insurance contributions, provided the premiums are not paid under a salary sacrifice arrangement.

- Benefits arise free of income tax.

- Benefits do not count towards the Lifetime Allowance for pension purposes. (Although Lifetime Allowance charges no longer apply, the Lifetime Allowance is still relevant in determining the taxation of certain death benefits.)

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