GOWLING WLG

DEATH BENEFIT SCHEME TAX REFORM: HOW TO MAKE IT WORK FOR YOU

09 April 2019

A change to tax law on 6 April 2019 means that an often-overlooked statutory rule has been lifted; simplifying the tax efficiency of contributions paid to non-HMRC-registered group life assurance schemes. However, the change is not overriding. In order for sponsoring employers and trustees to make best use of it, they should review the trust provisions and rules of their scheme and decide if an amendment needs to be made.

If you are an employer who provides death benefits for your employees via an 'excepted' group life assurance scheme, or if you are the trustee of such a scheme, you are likely to be affected by this simplification of the law.

Employers and trustees of HMRC-registered life assurance schemes are **not** affected by this change.

This insight explains what the simplification is, how it has come about and what employers and trustees can do to make sure that they make the most of it.

Key action points for employers and trustees

1. Identify how the rules restrict potential recipients

Employers and trustees of excepted group life assurance schemes should identify how their trust deed and rules restrict a member's range of potential recipients of death benefits.

2. Determine whether an amendment is required

After reviewing the rules, employers and trustees can decide if those provisions are already wide enough to accommodate the new tax simplification, or if an amendment is needed.

3. Consider member communications

Members may need to be warned that their existing death benefit nominations cannot be acted upon by the trustees, OR notified of the amendment being made to extend the range of members' potential beneficiaries.

What is the background to the reform?

Where an employer provides death benefits through a discretionary life assurance trust, the employee will often be asked to nominate beneficiaries to who they wish to have benefits paid upon their death.

Tax law has imposed an outdated, but still important, restriction on the way that non-HMRC-registered (or 'expected') group life assurance schemes provide their death benefits. It means that, if contributions to the scheme are to be made tax-efficiently, the range of potential beneficiaries that the member can nominate must be limited in a way that has not kept pace with modern life.

That limitation may have been overlooked by employers in the past. Its reform will permit members to choose from a wider range of potential beneficiaries when considering who will receive their death benefit and better ensure that employers and members continue enjoying the intended benefit in kind tax advantages granted to employer contributions under tax law.

It may be necessary for employers and trustees to amend their trust's rules to bring them in line with the new tax law.

Employers and trustees of HMRC-registered life assurance schemes are not affected by this change. This is because exemption from benefit in kind tax is already granted under a separate tax statute that does not impose the same restrictions.

Reform of the conditions for paying tax-exempt

employer contributions into excepted group life assurance schemes

On 6 April 2019, the Finance Act 2019 removed an old but often overlooked quirk of the law applying to the tax treatment of employer contributions to excepted group life assurance schemes. Previously, employers who made these schemes available to their employees were required to recognise an anachronistic statutory rule in order to ensure that contributions were exempt from income tax.

Contributions would only be tax-exempt if the beneficiaries of the trust (that is, the person to whom a benefit would be paid in the event of a member's death) were members of the deceased's 'household or family'. If they were not, the premiums paid by the employer would instead be treated as a taxable benefit in kind.

The current statutory definition of 'family' covers spouses, civil partners, parents, children and dependants - a perfectly normal, if slightly narrow, range of possibilities. But the definition of 'household' introduces the possibility of paying benefits to the member's domestic staff and house guests. It is conceivable, perhaps, that there might still be some homes in the UK where Jeeves or another faithful servant may be considered worthy of a stipend following the death of the head of the household, but we doubt that there are many. As a result, following lobbying from the group insurance industry (including Group Risk Development (GriD), an independent body of which Gowling WLG is a member), HMRC has recognised this and finally brought the provision out of the 19th century.

What has changed?

Finance Act 2019 has amended the Income Tax (Earnings and Pensions) Act 2003 with effect from 6 April 2019, replacing the old reference to family and household, so that the provision of death benefits from excepted group life assurance schemes will not be liable to income tax as a benefit in kind where those benefits will be paid to an **individual or registered charity**.

This simplification of the range of potential beneficiaries is a positive measure, encompassing the previous definitions but allowing trusts to recognise a much wider range of possible beneficiaries of the deceased member. It has been introduced with the aim of enabling excepted group life assurance schemes to remain relevant in the 21st century and promoting equal treatment regardless of the beneficiary's relationship with the member. Extending the exemption to allow members to nominate a registered charity is also consistent with the range usually provided to members of HMRC-registered schemes.

Why does it matter?

The old law was recognised as being largely unworkable and out of date, but it still had an effect on how death benefits were to be paid from many excepted group life schemes and the taxation of contributions to those schemes.

Many trusts' governing deeds and rules will be worded so as to adhere to the old definition precisely. Others (including those based on insurer-provided model documents) may have provisions that are written widely enough to accommodate the simplification already, but if they are not, an amendment might still be needed to allow for it.

Who is affected and what steps should they take?

Sponsoring employers of excepted group life assurance schemes will want to consider how the provisions of their current trust deed and rules restrict the range of potential beneficiaries of a death benefit and whether they wish to recognise the new tax reform. Remember: the new law is not overriding - individual scheme rules may need to be amended if they are to incorporate the simplification.

Trustees of those schemes should be aware of the range of potential beneficiaries within which they must work already, when determining to whom a death benefit can be paid. Should the sponsoring employer decide that a change is to be implemented to reflect the new simplification, the trustees' consent to a formal rule amendment may be required first.

Employees and their beneficiaries have an interest in the matter too, as current rules may still place a previously unappreciated restriction on who can receive a death benefit. Employers and trustees should check to ensure that existing rules on the range of potential beneficiaries are clear, understood and in line with expectations. If the scheme's rules are more restrictive than the trustees and members have been led to understand, it may be necessary to communicate this to members and for revisions to be made to existing nomination forms. On the other hand, if a change is made to recognise the new simplification, this should also be communicated to members in case it prompts them to review and update any nominations they may have made previously.

What are our recommended actions?

We have conducted a review of insurer-provided model documents and a range of bespoke trusts and concluded that many already have wording that is wide enough to accommodate the tax law simplification.

However, not all trusts have this, and in some cases, the trust's range of potential beneficiaries could benefit from considerable modernisation in order to better meet member expectations and comply with tax laws.

The introduction of this new simplification is a good reason for employers and trustees to re-familiarise themselves with their scheme's provisions and obtain the experienced views of their benefit consultant and legal adviser if they unsure of how the new law might affect their scheme.

Gowling WLG's pensions and employee benefits team has the technical know-how and industry links needed to help guide you through this matter simply and efficiently.

Related Pensions, Employment, Labour & Equalities

Author(s)

Kevin Gude

Legal Director - Associate of CILEX, London

Email

kevin.gude@gowlingwlg.com

Phone

+44 (0)20 7759 6878

vCard

Kevin Gude

Ben Goldby

Principal Associate - Birmingham

Email

ben.goldby@gowlingwlg.com

Phone

+44 (0)121 393 0262

vCard

Ben Goldby