

VitalityLife Business Protection

Case Study – Relevant Life Policy – Buttonit Ltd

At VitalityLife, we recognise that Business Protection can seem complicated. This case study involves a set of circumstances that may be similar to many of your clients' and explains the choices to be made when placing their VitalityLife Relevant Life Policy into trust. Also available on our website is a completed Relevant Life Policy Trust form using the facts of this case study as an example of how to fill in the Relevant Life Policy Trust deed.

1. Background

Buttonit Ltd is a successful button manufacturer. It relies heavily on the manufacture and supply of its new blazer button. The man in charge of the production line (with unique knowledge of how to maximise production and minimise cost) is Roy Fastener. If something happened to Roy, the business would suffer severe disruption with consequent significant financial loss. Buttonit Ltd have dealt with this by setting up key person cover.

Buttonit Ltd is, however, also concerned that Roy could be tempted away to its competitor, Zipper Ltd, and that could have

an equally damaging effect on the business.

Buttonit Ltd therefore wishes to provide Roy with the best employee benefits package possible so that it would be difficult for him to decide to leave and reward him for his hard work. Roy is not a shareholder in, or director of, Buttonit Ltd.

With this in mind, Buttonit Ltd have set up a good pension scheme for Roy and while this will provide a reasonable level of death-in-service benefits, it wishes to make provision for Roy's family should anything happen to him – and in a tax-efficient way.

2. Dealing with the financial needs

- (a) Set up a VitalityLife Relevant Life Policy on Roy's life.

Buttonit Ltd choose a sum assured of £200,000 (up to 15x salary is available) with a term expiring when Roy is 65 – his anticipated retirement age. The policy includes death benefit and terminal illness benefit. Vitality is not included as this is not permitted under the tax relief rules.

- (b) Under the Relevant Life Policy trust, Buttonit Ltd is the initial trustee and it can appoint other trustees – including Roy's adult relatives. Roy and his close family are beneficiaries. This means that terminal illness benefits could be paid to Roy. In the event of his death, death benefits are to be paid to Roy's widow or children. With this in mind, Roy can sign a non-binding (and changeable) Letter of Wishes indicating to whom he would wish the trustees to pay death benefits to.

As well as providing the necessary level of death benefits, the Relevant Life Policy arrangement is taxed in a very favourable way:

- (i) Premium payments
- These are deductible for the employer.
 - The premiums are not assessed as a benefit on Roy.
- (ii) Policy proceeds
- No income tax is payable on the policy proceeds if Roy dies and they are paid to the trustees of the Relevant Life Policy trust.
 - The payment of premiums would not be gifts with reservation of benefit from an inheritance tax standpoint because they are paid by the employer company.

- No inheritance tax is payable on the policy proceeds when they are paid to the trustees.
- (iii) Payment out of the trust by the trustees
 - Terminal illness benefits (if applicable) can be paid to Roy or the beneficiaries under the trust.
 - Death benefits will be paid by the trustees to the beneficiaries under the trust - probably following a letter of wishes from Roy.
 - Payment of benefits could trigger an exit charge for inheritance tax. However, there is unlikely to be a charge unless the trust fund had

some considerable value on the last ten-yearly anniversary.

For that to be the case Roy would have needed to be in seriously ill health (or the policy proceeds had already been paid on Roy's death).

- If terminal illness benefits are paid to Roy they would then form part of his taxable estate for inheritance tax purposes. So it would probably be best for the trustees not to exercise their discretion in favour of him and pay these benefits to him unless it can be guaranteed that he will spend them whilst alive.

3. The Plan in action

Two days after Roy's 57th birthday he dies after suffering from a heart attack.

£200,000 is paid under the VitalityLife Relevant Life Policy to the trustees, free of income tax and inheritance tax. Buttonit Ltd appoints Roy's widow and brother as trustees. Buttonit Ltd is then removed as a trustee and so Roy's family have control over the trust fund. In accordance with Roy's

Letter of Wishes the trustees pay £100,000 of the death benefit to his widow, Raquel, and £50,000 each to his two daughters, Britt and Sonia.

Because the Plan was set up 12 years ago an inheritance tax exit charge could arise. However, no charge arises as Roy was previously in very good health.

4. Completing the trust forms

The directors of Buttonit Ltd would need to complete an application on behalf of the company for a VitalityLife Relevant Life Policy on Roy's life. Roy would need to complete a health questionnaire.

Buttonit Ltd would need to complete the Discretionary Trust (for use with a Relevant Life Policy) document as follows:

- In Part A, Buttonit Ltd would insert the date of the Trust with the same date as the application form for the Relevant Life Policy.
- The employer, Buttonit Ltd, would also insert its full name and address in Part A.
- In Part B, Buttonit Ltd would complete details of the Policy. This would include the date of the application and the full name of the Life Assured ie.

Roy Fastener (the employee for whose benefit the Plan is being established).

- In paragraph (iii) of Part C, full details of the Default Beneficiaries (and the shares in which they are to benefit) should be inserted. These are the beneficiaries who will benefit if no other appointment is made under the trust. For example, when the trust proceeds remain in the trust on the 125th anniversary of the trust deed. Typically, the Default Beneficiaries will be the people that Roy would ultimately wish to benefit. In this case, this is Raquel Fastener (wife), as to 50% of the trust fund, and his two daughters, Britt and Sonia, as to 25% of the trust fund each.
- In Part I, the authorised officials of Buttonit Ltd would sign the trust deed on behalf of Buttonit Ltd and their signatures witnessed.

Relevant Life Policies from VitalityLife gives your client's employees discounts and rewards on things that are good for them. Allowing your SME clients to offer their employees big business benefits.