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**PDQ**

# HMRC clarifies position on fixed protection and life assurance

Following our **recent note** about life assurance for high earners taking fixed protection after 6 April 2012, HMRC have issued a formal statement in response to representations made by the pensions industry.

However, depending on a particular scheme's rules and the insurance policy backing the benefit, fixed protection could potentially still be lost following payment of an insurance premium.

### What HMRC are now saying

HMRC's revised position is as follows:

1. Where the only death benefit payable for fixed protection members after 6 April 2012 under a registered scheme's rules is an amount equivalent to what is paid under an insurance policy, this is a money purchase (defined contribution) arrangement and so any contribution or premium paid after 6 April 2012 will therefore result in fixed protection being lost.
2. Where the death benefit payable for fixed protection members after 6 April 2012 is expressed to be the **greater** of a defined benefit (eg 2 times pensionable salary at the date of death) **or** the amount payable under an insurance policy, HMRC's view is that this is a hybrid arrangement and so the payment of a premium will result in fixed protection being lost.

However, the following situations will not be counted as money purchase or hybrid arrangements, there will not be any benefit accrual and premiums paid after 6 April 2012 will not cause fixed protection to be lost:

1. Where the only benefit payable for fixed protection members is a defined benefit (eg 2 times pensionable salary at the date of death); or
2. If the amount payable under an insurance policy in excess of the defined benefit is retained by the scheme; or
3. Where a defined benefit is payable and the scheme makes up the shortfall in the amount paid by an insurance policy; or
4. Where a defined benefit is payable, is backed by an insurance policy and the policy contains restrictions which may mean, if they apply, that a **lesser** amount will be paid to the scheme or beneficiaries than the full defined benefit. HMRC have in mind here catastrophe event restrictions and restrictions on particular individuals who represent a greater risk which are common in life assurance policies.

However, HMRC then go on to say that the restricted amount, after the restriction is applied, should still "itself be expressed as a defined benefit lump sum death benefit" (i.e. an amount determined by reference to salary, service of the member or some other factor). They give examples of this:

- the benefit represents a percentage of the [defined benefit] that would have been provided in normal circumstances
- it is paid on a pro rata basis
- it is expressed as a lower amount
- the maximum paid under the policy is capped

5. Where a refund of contributions is payable on the member's death. (Where the rules also provide for the refund to include interest, this must be expressed or can be expressed in percentage terms).

## Clyde & Co comment

HMRC's clarification is likely to have reduced the number of schemes which will be impacted by their previous interpretation. It is therefore useful to have.

However, the requirement in HMRC's note that the actual amount paid under paragraph 4 can still be "expressed as a defined benefit" lump sum is slightly circular and it is not completely clear what it means. It suggests, however, that they are not giving a complete waiver for those situations where a lesser amount than the full death benefit based upon a multiple of salary is paid to the beneficiary because of restrictions in the policy.

The question of whether fixed protection may be lost on payment of a premium after 6 April 2012 is therefore likely to depend on the particular scheme rules **and** the terms of the particular insurance policy and both will need to be considered carefully. If there is an issue for a particular scheme, the option of setting up an excepted group life policy trust or ensuring that only pure defined benefits (i.e. a multiple of salary) would seem to remain the ways forward to avoid losing fixed protection.

As fixed protection is only lost on the payment of the premium, those schemes which are planning to set up an excepted group life policy may have some more time if no premium payment is due in the near term.

HMRC have remained resolutely silent on whether those with enhanced protection may also be subject to a similar issue.

**Further information**

If you have any questions or want a review of how your life assurance arrangement can affect fixed protection please contact:

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Further advice should be taken before relying on the contents of this summary.