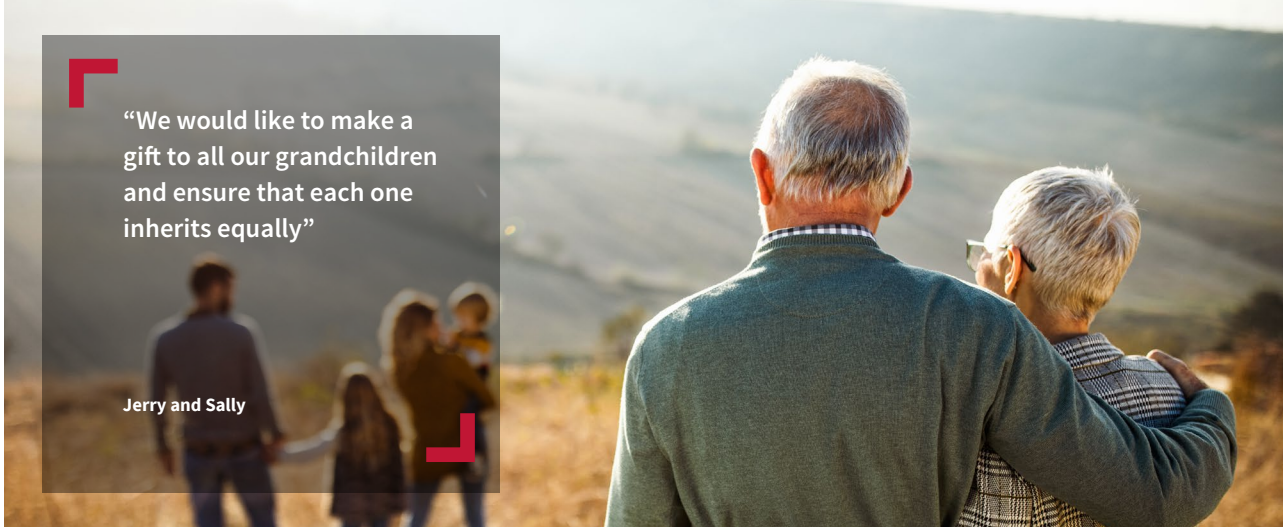
canada life™

Benefits of segmentation

Case study 1



The facility to segment an investment bond using a series of individual identical policies is an attractive feature that can provide added flexibility and tax efficiency.

Jerry and Sally:

- Are aged 74 and 72 respectively
- Have combined assets worth £2.5 million
- They have 10 grandchildren (ranging from 5 to 15 years) and have been told that no more are planned
- They invest £600,000 into a Premiere Account and place it under a discretionary trust

Having spoken to a financial adviser Jerry and Sally like the idea of the Premiere Account, written under a discretionary trust, as this allows them to ring-fence individual policies for each grandchild.

Once Jerry and Sally have lived for seven years after setting up the trust, it will not be included in their estates for inheritance tax purposes. However, as the trust is discretionary in nature it is within the Relevant Property Regime for inheritance tax purposes, potentially subject to ten year and exit charges, where the value of the bond exceeds the available nil rate bands at each relevant point.

As Jerry and Sally have gifted more than 80% of their individual nil rate bands the trust is more likely to have these charges, so an Inheritance Tax account (IHT100) will need to be returned to HMRC. In addition, the trust will need to be registered on the Trust Registration Service. See **Relevant Property Trusts - the reporting requirements** and **TRS hub** for more details.

As the Premiere Account can have up to 99,999 individual policies with no minimum premium the financial adviser suggests the bond is set up with 99,999 individual policies, each with a premium of £6. This means that the trustees can ring-fence 9,999 individual policies for each grandchild which will help the trustees with administration.

Three years later their first grandchild, Kerry, starts university. As university tuition fees in England and Wales can be as high as £9,250 each year the trustees would like to make sure she is not burdened with a substantial student loan for years to come.

Each individual policy, assuming 3% annual investment growth, has grown to £6.37. The adviser calculates that the trustees need to cash in 1,453 of Kerry's allocated policies for a surrender value of £9,255.61 (1,453 x £6.37), giving a chargeable gain of £538.

But he emphasises to the trustees that they must appoint the policies into a bare trust for Kerry before cashing them in. For tax purposes Kerry, as the absolute beneficiary, is liable to any income tax and as she has no other income, she will have an unused personal allowance in addition to, the £5,000 starting rate savings band and her £1,000 personal savings allowance.

For the next subsequent two years the trustees assign 1,410 and 1,370 individual policies respectively to Kerry for her university fees. At the end of Kerry's three year course her university fees have been paid and her remaining allocated policies are 5,766.

The trustees have discretion who to pay and being able to ring-fence individual policies for particular beneficiaries gives the trustees the ability to manage the trust fund to ensure that all beneficiaries are treated fairly. The trustees would need to consider if there is an IHT exit charge when distributions or appointments are made to the trust beneficiaries. Generally, there would be no exit charge on appointments or distributions made in the first ten years if there was no 'entry charge' to IHT when the trust started.

For more information on the benefits of segmentations, please contact your professional adviser.

This document is based on Canada Life's understandings of applicable legislation, law and current HM Revenue & Customs practice as at November 2023. It is provided solely for general consideration. The information regarding taxation is based on our understanding of current legislation, which may be altered and depends upon the individual financial circumstances of the investor. We recommend that investors take their own professional tax advice.

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