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# Whole of life assurance

November 2013

## Case study

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## Introduction

There are tremendous opportunities for advisers in the protection space. The protection gap is well documented and, post-Retail Distribution Review (RDR), advisers not registered to give investment advice (ICOB registered advisers) as well as investment advisers have the option to grow their protection book and add value to their businesses.

Against this backdrop, whole of life assurance products such as Scottish Provident's Pegasus plan are being promoted as an effective way to address client needs. Advisers should look again at whole of life not just for inheritance tax (IHT) planning but for lifestyle protection, asset preservation and wealth creation.

Whole of life assurance has a chequered past. The unit linked product feted by advisers in the 1980s as the ultimate financial planning solution was promoted as offering both protection and an investment in one plan.

It fell from favour but remained available as an IHT planning tool. RDR has dealt the unit linked product another blow making it subject to adviser charging as an investment product.

This has caused providers such as Scottish Provident to reinvent their whole of life plans as protection-only products.

Jennifer Gilchrist, Senior Product Development Manager at Scottish Provident, said of the new Pegasus plan:

*"We've removed the investment element which will allow ICOB-registered advisers, as well as investment advisers, to recommend it. As the emphasis on providing holistic financial planning continues to gain momentum, the focus on multi-usage whole of life will grow."*

This case study will examine and explain the uses and benefits of recommending whole of life assurance. It will help to encourage readers to consider client needs beyond immediate protection requirements in order to add value to both their own business and their clients' protection plans.



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It will also enable advisers to identify distinguishing features of products and propositions by using Scottish Provident's Pegasus plan as a benchmark for product research and comparison.

A handwritten signature in black ink that reads "Ben Heffer".

**Ben Heffer**

Insight Analyst,  
Life & Protection

## Whole of life in context

Unlike term assurance, which pays out on the death of the life assured during the term of the policy, whole of life assurance pays out on death whenever it occurs. This makes it a more effective solution for lifestyle protection in many circumstances. Traditionally, whole of life policies included an investment element, which was used to help fund the increased cost of cover in later life, to provide greater benefits on death, or an early surrender value.

### With-profit whole of life

A minimum level of benefit on the death of the life assured is established at outset. Reversionary bonuses are added to the policy each year, which increase the final pay out. On death, a terminal bonus may also be paid increasing the benefit still further. Such policies have the advantage of covering the full liability from the outset and providing an element of inflation proofing by way of the bonus allocation. This type of plan probably represents the most expensive whole of life option.

### Low cost whole of life

The policy has a guaranteed sum assured. However, at outset a lower sum assured is specified, which is the basis of the reversionary bonus calculation. On death the pay-out will be the greater of the guaranteed sum assured and the basic sum assured plus bonuses. The plan is structured by combining a with-profit savings plan with a decreasing life assurance element to maintain the guaranteed sum assured. Low cost whole of life is typically cheaper than with-profit whole of life, reflecting the lower benefit levels.

### Unit linked whole of life

By far the most popular form was unit linked (or flexible) whole of life. At its height in the mid-1990s, there were as many as 70 products from 50 providers; subject to gradual decline, by November 2012 this had reduced to just seven plans from three providers. Now as a result of RDR only one of these products remains and it does not accrue a surrender value.

Premiums were used to buy units in one or more unit-linked insurance funds. At outset, the client could choose the level of life cover they required between a maximum and minimum level. Each month units were encashed to pay for the life cover for the following month. Those requiring a lower level of life assurance thereby accrued a higher investment fund because fewer units were encashed; those requiring a high level of life cover accrued a smaller investment element. The policies were flexible because the level of life cover could be varied to take account of changing circumstances. Under RDR, policies with an investment element can only be sold by qualified wealth managers and are subject to adviser charging. Consequently, providers have moved away from unit linked whole of life to cater for pure protection advisers that do not wish to adopt adviser charging.

### Non-profit whole of life

Non-profit whole of life has no investment element and the premiums are calculated at a level necessary to pay for the life cover over the course of the policy. These premiums are usually guaranteed. The Pegasus plan offers both guaranteed and reviewable premiums.

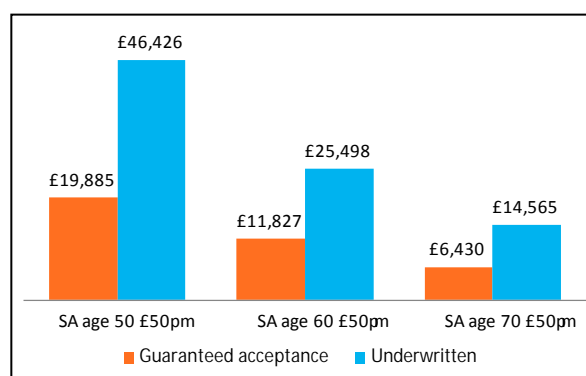


### Premium sustainability

The non-profit option offers surety for advisers in the face of many difficult 10 year reviews with clients where either premiums have had to increase and/or sums assured have been reduced to take account of the mismatch between actual unit linked fund performance and that forecast at outset. Pegasus, with its guaranteed rates, tackles this very issue, which has quite unfairly tainted whole of life assurance in financial planning.

Advisers should note that the Financial Ombudsman Service is seeing an increase in complaints about whole of life assurance. There were 3,241 complaints about whole of life and savings endowments in the year 2012/13, an increase of 18% on the previous year. The principal complaint is that it was not made clear at the point of sale that the premiums would increase (or the benefits decrease) at review. However, it should also be noted that many of these were speculative complaints from claims management companies and that the uphold rate was only 23%. Reviewable premiums are applicable and represent good advice in the appropriate circumstances but advisers should always take great care to explain the nature of reviewable whole of life and document their advice accordingly.

These policies have the potential to be bad value for money should the insured survive for a long time after inception as the total premiums paid could exceed the value of the death benefit. Most guaranteed acceptance policies are sold direct and are frequently incentivised by a 'free' gift or high street vouchers. They are popular and demonstrate an appetite for cover. For clients in reasonable health however, the underwritten route should be considered and advisers have the opportunity to add value in helping to arrange cover. The following chart shows the potentially greater sums assured available per pound of premium by pursuing the underwritten route for clients; typically in excess of double the cover is available.



Source: Guaranteed acceptance plan premiums - Defaqto; Non-profit whole of life premiums - Avelo.

### Guaranteed acceptance plans

Guaranteed acceptance plans are non-profit whole of life assurance policies specifically designed for the over 50s market. Applicants for these policies are not underwritten. Instead, the policy will exclude claims for death by natural causes in the first one or two years. Most policies now have a premium cap such that premiums are paid only up to a certain age, although a small number of policies still require premiums to be paid throughout the policy.

## Trusts

According to some estimates as few as 6% of life assurance policies are written in trust and yet, where appropriate, this is an essential part of effective financial planning.

There are essentially three financial planning advantages to writing policies in trust. Firstly, on death, claims from policies held in trust are paid out without having to await probate so the client's dependents get the benefits promptly. Secondly, the client can maintain control over who receives the benefits and thirdly, in many cases the policy proceeds can be kept out of the client's estate for inheritance purposes, thus avoiding having to pay tax unnecessarily.

Even if the resulting decision is not to write a policy in trust, advisers should always consider whether or not it is appropriate.

### Bare trusts and discretionary trusts

Under a bare trust, all the benefits pass to the beneficiaries named in the trust deed. Once set up, the named beneficiaries cannot be changed although, of course, the client can lapse the policy. Under a discretionary trust, the trustees decide who should receive the benefits from a list of potential beneficiaries included in the trust document taking into account the client's intentions with reference to an 'expression of wish' letter. The client can subsequently change the beneficiaries and for this reason these trusts are sometimes referred to as flexible trusts.

Scottish Provident's Gift Trust allows beneficiaries to be added by the donor at a later date.

The use of split trusts has become less significant for whole of life because they are primarily associated with policies including both life and critical illness cover and very few whole of life contracts now offer critical illness insurance.

Scottish Provident's Gift Trust can be established as a discretionary trust or a bare trust and is suitable for use with the Pegasus whole of life plan, where appropriate.

### Taxation of trusts for IHT purposes

The Finance Act 2006 established a new regime for the treatment of trusts for IHT purposes in that lifetime gifts to discretionary trusts (those where the donor maintains on going control of the distribution of the assets) can be liable to IHT. This means that, whilst prior to 22 March 2006 life policies placed in trust were rarely caught by IHT, those placed in trust since can be subject to charges in certain circumstances (see Appendix for the details of the potential charges). Bare trusts are not affected by this change but are less flexible for clients and even if charges are incurred, that may still be preferable to suffering a 40% charge on the estate.

○ As few as 6% of life assurance policies are written in trust and yet, where appropriate, this is an essential part of effective financial planning. ○

### Scottish Provident can help

Scottish Provident can provide assistance with choosing the right trust for a client's circumstances and has a range of trusts that can be used in conjunction with its protection plans including Pegasus whole of life assurance.

	Bare Trust	Discretionary Trust	Suitable for new Pegasus Plans (life only)	Suitable for existing Pegasus plans with critical illness cover
The Probate Trust	✗	✓	✗	✓
The Gift Trust	✓	✓	✓	✗
The Split Trust	✓	✓	✗	✗
The Business Trust	✗	✓	✓	✓

The Probate Trust is a discretionary trust that is suitable for policies that include life and critical illness or disability benefits. It enables the benefits to be paid to the appropriate persons (including the policyholder) promptly avoiding probate but does not mitigate inheritance tax. New Pegasus plans are purely for life cover, so a Gift Trust would normally be preferable.

The Gift Trust is primarily used for policies with life assurance benefits only.

The Split Trust, which can be used very effectively with life and critical illness term assurance policies, is not suitable for Pegasus plans that included both life and critical illness benefits where there is either a separate death benefit or a buy-back option because HMRC considers such an arrangement to be a gift with reservation of benefit for IHT purposes.

The Business Trust is a discretionary trust to facilitate the tax efficient payment of shareholder/partnership protection policy proceeds. The Gift with reservation rules do not apply as these policies are regarded as commercial arrangements rather than gifts for IHT purposes.

IO Advisers should always consider whether or not it is appropriate to write a policy in trust. OI



## Opportunities for whole of life in financial planning

This section sets out the financial planning opportunities for whole of life assurance post-RDR for lifestyle protection in both the personal and corporate planning arenas. For corporate business, it identifies how whole of life can accommodate succession and continuity planning.

It illustrates how the non-profit or guaranteed whole of life plan can be very effective and more appropriate than pure term in many instances; particularly now that many clients are taking on liabilities later in life. It also looks at how whole of life assurance can be used effectively for estate planning, asset preservation and wealth creation purposes.

### Lifestyle protection

Most couples and families have a need for life assurance so that if one income provider dies unexpectedly the lost salary or pension income can be replaced, thereby protecting the family's lifestyle.

Where the requirement is for lifestyle protection alone, whole of life assurance provides a more flexible approach than term assurance. In reality the need for lifestyle protection does not necessarily cease at retirement and, with the demise of the concept of normal retirement age, a more flexible solution is often required. Whole of life assurance, by definition, has no end date so even if the requirement for cover diminishes the client still has continuing insurability. Conversely, once a term assurance policy ends, further cover will be subject to medical underwriting and by then the client will be older and their health may have deteriorated.

The Pegasus plan can be set up on a standard guaranteed premium basis where the premiums are calculated at the level needed to keep the chosen level of cover throughout life. Alternatively, the maximum cover basis utilises reviewable premiums, which are reviewed for the first time after 10 years and at five-yearly intervals thereafter. The maximum basis provides the highest level of cover for the lowest initial premium.

The initial recommendation should be to cover the client's shortfall, over the duration of need. Standard cover is most suitable for this; however, where the budget for standard cover is insufficient to meet the full requirement, the adviser can consider using the maximum cover basis. Although the level of cover is unlikely to be maintained for life without an increase in premium, the necessary cover will at least be in place initially.

The following table demonstrates the competitiveness of whole of life written on a maximum cover basis compared with 10 year term assurance. The premiums are set at a similar level but whole of life offers continuing insurability and the opportunity to maintain cover levels by paying a higher premium. Premiums in later years will increase significantly.

£100,000 benefit	Pegasus Guaranteed Premiums (p.m)	Pegasus Reviewable Premiums (p.m)	Average 10 year Term Assurance Premiums (p.m)
Non-smoker aged 40	£75.20	£15.33	£10.33
Non-smoker aged 50	£115.87	£23.61	£19.38
Non-smoker aged 60	£185.72	£58.07	£48.88

■ Cost comparison of whole of life and term assurance. Source: Avelo.

Naturally the sustainability of maximum cover, at the end of the client's review period, should always be taken into account when making a recommendation. With this in mind, consideration should be given to the client's earnings potential. For example, a customer may be in a profession where there is a realistic expectation of increased earnings, in which case maximum cover can be justifiable on the grounds that funding for increased premiums will be available later on. With this in mind, the myth that whole of life assurance is a product suitable only for older people can be dispelled.

For lifestyle protection, whole of life assurance should be written in trust for the beneficiaries. This ensures that on death, they receive the proceeds quickly and in the most tax efficient way.

#### Increasing cover

Having established the right level of cover for lifestyle protection, it is important that it keeps pace with the increasing cost of living so that the cover retains its purchasing power.

When the Pegasus plan is set up an increasing benefit can be chosen, such that the sum assured increases each year in line with the Retail Prices Index, subject to a minimum of 2% and a maximum of 10%. Alternatively, indexation can be added at a later date subject to underwriting.

#### Debt protection

Where it is established that the client has a fixed liability, such as a mortgage or loan, the first recommendation may well be for a term assurance product of the appropriate duration. However, where the client also has continuing lifestyle protection needs a whole of life recommendation can more effectively address all the requirements.

Pegasus can be set up on a standard guaranteed premium basis to cover loans and fixed liabilities or, where affordability is an issue and the duration of the loan does not exceed 10 years, the maximum reviewable premium basis can be used. This will ensure that the liability is covered and provide valuable lifestyle protection thereafter, subject to review.

Whilst it is good practice to write life assurance in trust, it is not appropriate to do so where a policy is set up to repay a debt and is assigned to the lender. If the policy is unassigned, consideration should be given to using a discretionary trust so that the trustees can pay the benefits to the lender if the debt is still outstanding or to the beneficiaries in accordance with the client's expression of wish.

## Business protection

Business protection represents tremendous opportunity for advisers to write more business while addressing the needs of their corporate clients. It is quality business characterised by substantial sums assured and multiple policy sales.

Pegasus plan has an unlimited maximum benefit and generous financial underwriting limits, particularly for those up to age 50. Additionally, free cover is available while the application is being processed.

Business protection comprises two elements: continuity planning, which includes key person and corporate debt protection; and succession planning.

### Continuity planning

Traditionally, advisers use term assurance plans to cover their clients' key people/employees. Not least, because in order to benefit from tax relief, the policy must either be an annual policy or short-term policy (five years or less); also policies written on the lives of directors with more than 5% of the company's shares will not benefit from tax relief. However, the financial loss to the company on the death of a key person can be significant. While choosing a tax efficient solution is important, it is more important to have the right level of cover in place; whole of life should at least be considered - particularly in the case of business owners and controlling directors who are happy to continue to work beyond what most would regard as normal retirement age. Additionally, premium sustainability may be less of an issue in the corporate sphere than in individual protection.

An important aspect of business assurance is the protection of corporate debt. Life assurance is written on the life of a person who has guaranteed a business loan. Also, banks sometimes make business loans on the basis of the involvement in the business of certain key employees. If such a key employee is no longer part of the business, the bank may want the loan to be repaid early. Additionally, it is common for directors to make loans to their companies. In all these scenarios whole of life assurance can be considered, particularly where the duration of the guarantor/lender's involvement in the business is undefined. As with individual cover, it is important to set up the plan on a standard basis so that the level of cover is fixed throughout the duration of the outstanding debt. Maximum cover could be considered if the term of the debt were 10 years or less.

Where the debt is repaid while the guarantor/lender is still living, the policy provides continuing insurability and may be useful as key person protection; alternatively, the policy can be assigned to the individual to provide him or her with personal cover.

IO While choosing a tax efficient solution is important, it is more important to have the right level of cover in place. OI

## Succession planning

Succession planning is another area in which it is worth considering a whole of life recommendation. When a shareholder or partner in a business dies, their share of the business normally forms part of their estate and ultimately passes to their beneficiaries.

In the case of a controlling partner or shareholder, this could mean the future direction and running of the business is dictated by people not closely associated with it and with no relevant expertise. A legal agreement is put in place giving the remaining partners or shareholders the right to purchase the shares, and the whole of life plan provides the funds to execute the agreement.

The way in which succession planning is arranged will differ depending upon whether the business is a limited company with shareholders or a partnership; there are a number of strategies that can be used. Insurers such as Scottish Provident that specialise in business protection can provide support for advisers helping them to choose the most appropriate strategy and putting the cross option agreements in place.

Scottish Provident is a specialist business protection provider offering help and support to advisers for business protection cases.

A significant proportion of businesses expect to buy the business owner's shares should he or she die prematurely but 73% of small businesses have no partnership or shareholder protection in place.<sup>1</sup>

Scottish Provident's Business Trust can be used to shelter the policy proceeds from inheritance tax and facilitate the purchase of the deceased partner or shareholder's interests by the remaining partners or shareholders.

## Estate planning

On death, an individual's estate in excess of £325,000 is liable to inheritance tax (IHT). Whole of life assurance is an effective way to mitigate the liability. A policy is written on the estate holder's life for the amount of the estimated liability and written in trust for the beneficiaries of the estate.

On death, the proceeds of the whole of life policy pass to the beneficiaries outside the estate and provide the funds to pay the inheritance tax bill. Given that many estates are principally made up of property, this not only protects inherited wealth but also avoids the beneficiaries having to realise assets at a less than convenient time. While HMRC permits IHT to be paid in instalments where the estate is in the form of property, if there is no IHT plan in place the beneficiaries may still have to liquidate property assets at a time of poor market value or take out expensive bridging loans to pay the outstanding tax.

There is no liability to inheritance tax between spouses so whole of life assurance is set up on a joint life second death basis. On the first death, the estate passes free of tax to the surviving spouse; on the subsequent death of the spouse the policy pays out to the beneficiaries.

<sup>1</sup> Source: Scottish Provident Small Business Risk Research - [www.scottishprovident-businessprotection.co.uk/what-is-business-Protection/partnership-and-shareholder-Protection.aspx](http://www.scottishprovident-businessprotection.co.uk/what-is-business-Protection/partnership-and-shareholder-Protection.aspx)

In February 2013, the government announced that the current IHT threshold would be frozen at the current level until at least 2019. It is estimated that 5,000 extra families per year could be caught by inheritance tax as a result. Additionally, the rules governing the deductions against outstanding debts on the estate have been tightened up. IHT was charged on the net value of the estate after deducting outstanding liabilities at the date of death. In future, a deduction will only be allowed to the extent that the liability is repaid to the creditor from out of the estate. This has implications both for individual and business protection scenarios and means that more people will have to think carefully about their liability to inheritance tax than previously.

On average, inheritance tax bills are in the region of £95,000. It is definitely worth advisers examining the inheritance tax position of their clients. Advisers should check that clients have written wills and that they are reviewed regularly.

Pegasus can be written on a single life or on a joint life basis, as required. Joint life policies can be set up to pay out on the first death, which is suitable for lifestyle protection, or on the second death, which is suitable for estate planning. Scottish Provident's Gift Trust set up on a discretionary basis can give maximum flexibility and in most cases avoid a large inheritance tax bill.

One of the key requirements in estate protection is the ability to change the cover to take account of a higher liability. Advisers should review their clients' circumstances regularly to ensure their liabilities are still covered. Consider recommending a policy with guaranteed insurability options.

Pegasus offers a range of guaranteed increase options facilitating an increase in cover without further medical underwriting on the occurrence of certain events, including an increase in IHT liability.

Under the Pegasus inheritance tax increase option, the benefit amount can be increased on more than one occasion up to an overall limit of the lower of 50% of the original benefit amount and £250,000.

The option can be exercised if inheritance tax liability increases due to an increase in value of the client's estate or if legislative changes increase inheritance tax liability. No further medical underwriting will be required, but the revised premium will take into account the premium rates and age of the life assured at the time.



## Wealth preservation and creation

Whole of life assurance is an important tool to help clients preserve the value of their assets for future generations.

Paying out on death whenever it occurs, the benefit can be used to replace any calls on the client's wealth associated with death and later life, for example, funeral and testamentary expenses, care home fees, and general living expenses that eat into savings and investments.

### Maximising pension benefits

When individuals come to annuitise their pension pots, the selection of dependants' benefits will significantly reduce the amount of pension they can receive. Rather than purchase dependants benefits via an annuity, it may be desirable to purchase a single life annuity and insure the spouse's benefits by setting up a whole of life assurance plan. While this will not necessarily be a more cost effective route there are certain advantages. In the event that the dependant's benefits are not required (for example, the dependant spouse dies first), dependant's benefits purchase through the annuity would be lost but the whole of life plan will still add additional value to the estate when the policy holder dies. Whole of life assurance is a key tool in maintaining cash flow in the post-retirement phase of financial planning.

## Long-term care

The funding of long-term care for elderly people is controversial. People are generally living longer but not necessarily healthier; the state is ill equipped to meet the cost of the spiralling care bill and many regard it as reasonable for the wealthy (and not so wealthy) to utilise their assets to pay for care. Conversely, many want to preserve the value they have built up in their property and other assets to pass on to their children when they die.

Writing a whole of life plan in trust for the beneficiaries can help replace the assets that need to be encashed to pay for care.

According to a study by Herefordshire County Council in 2013, the average length of stay in long-term residential and nursing care in 2011/12 was 121 weeks. The average cost of a residential home is £580 per week and £700 per week in a nursing home. This represents a drain on the client's assets of as much as £84,700 and possibly much more if they have a longer stay in a home.

A joint life second death Pegasus plan for £100,000 covering a couple aged 60 costs £119 per month on a standard basis and £19 per month on a maximum basis.

■ Source: Avelo. 01/11/2013

Based on the average care home costs and length of stay referred to above, the following cost benefit analysis demonstrates how whole of life can preserve the value of the estates for persons dying at age 80 and age 90.

	No whole of life plan	Whole of life £100,000 last survivor dies at age 80	Whole of life £100,000 last survivor dies at age 90
Value of estate at age 60	£300,000	£300,000	£300,000
Less care costs	(£84,700)	(£84,700)	(£84,700)
Less whole of life premiums	N/A	(£28,560)	(£42,840)
Plus whole of life benefit	N/A	£100,000	£100,000
Value of estate on death	£215,300	£286,740	£272,460

Based on a guaranteed whole of life premium of £119 per month for couple aged 60.

### Funeral expenses

One of the traditional uses of whole of life assurance is to cover funeral expenses. Many people do not wish their loved ones to be burdened with the sometimes prohibitive costs of a funeral and this remains one of the main drivers for the popularity of guaranteed acceptance plans, some of which are specifically designated as funeral plans.

While funeral expenses planning may not be a significant need for high net worth clients, it is a way for advisers to add value for less well-off clients. Arranging whole of life assurance to meet this need has distinct advantages over a funeral plan or guaranteed acceptance plan bought direct.

Research by Which? in 2012 found that the increasing cost of funerals outstrips the indexation employed in most funeral plans leaving a shortfall<sup>2</sup>. Also, a similar piece of research in 2013<sup>3</sup> identified that many plans typically don't cover third party costs, which make up a significant part of the bill. Third party costs include, for example, doctors' fees, fees charged by the church, the cost of grave digging and burial plots. With whole of life assurance a level of cover can be established to take into account as many of these services as required.

The underwritten plan is far more cost effective for covering funeral costs than a guaranteed acceptance plan. The average cost of a burial in the UK is in the region of £3,000. Assuming inflation of five per cent, this will be £4,887 after 10 years, £7,960 after 20 years and £12,966 after 30 years.

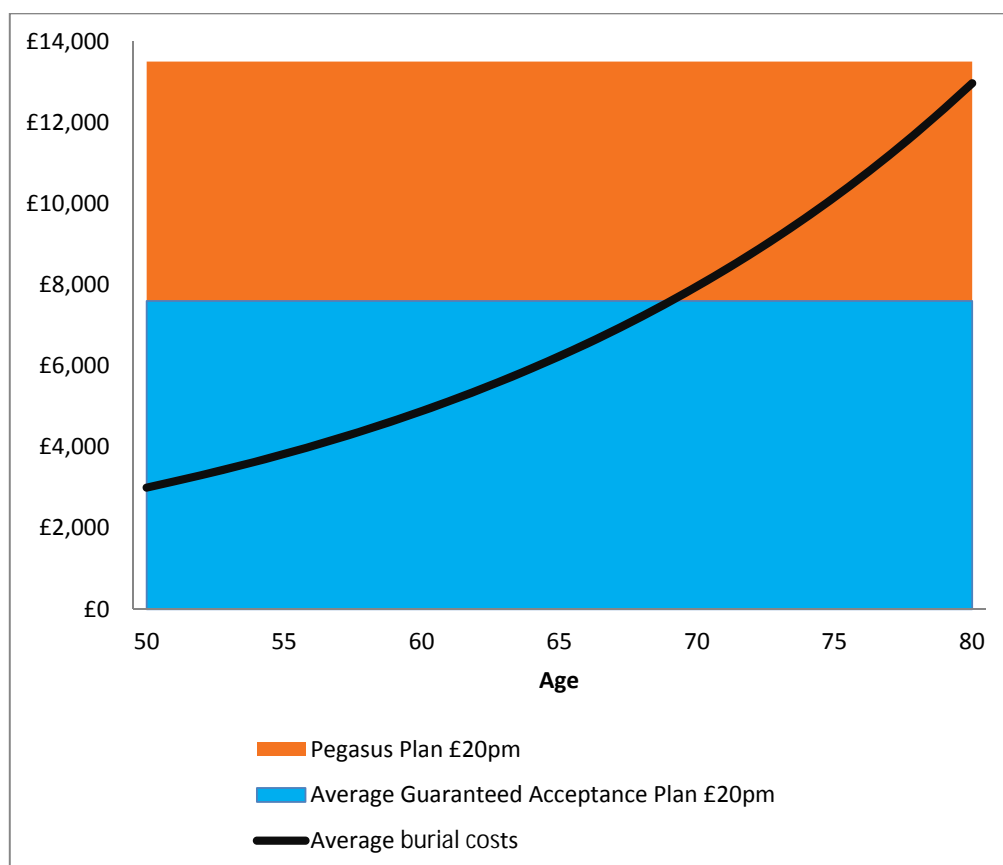
<sup>2</sup> <http://www.which.co.uk/news/2012/09/funeral-costs-increase-for-eighth-consecutive-year-295829>

<sup>3</sup> <http://www.which.co.uk/news/2013/09/funeral-costs-increase-by-80-since-2004-332334>

Guaranteed acceptance plans for someone aged 50 paying £20 per month provide on average a benefit of £7,600.<sup>4</sup> This means that the full cost of the funeral is unlikely to be covered if the policy holder dies after age 70.

By contrast, a 50 year old paying a premium of £20 per month to a Pegasus plan on a level guaranteed basis can secure a sum assured of £13,503.<sup>5</sup> This could cover the cost of burial up to age 80. Alternatively, the minimum premium of £10 per month secures benefits of £5,925, which can be increased each year to keep pace with rising costs.

The average total cost of a funeral including burial and third party costs now stands at £7,622 according the latest Which? report. This could rise to £32,942 over 30 years (assuming annual increases of five per cent). A 50 year old paying a premium of £40 per month to a Pegasus plan on a level guaranteed basis can secure a sum assured of £29,790,<sup>6</sup> which could cover the cost of the funeral up to age 76.



<sup>4</sup> Source: Defaqto

<sup>5</sup> Source: Avelo

<sup>6</sup> Source: Avelo

### Wealth creation

Another main driver for the market in guaranteed acceptance plans is the provision of a legacy for children and grandchildren. While this may involve quite modest amounts, many people wish to leave their loved ones something when they die.

The use of underwritten whole of life assurance plans opens up the possibilities to creating significant legacies, which can be written in trust for the benefit of specific beneficiaries.



## Checklist for whole of life opportunities

For clients with partners and/or dependants, after addressing their income protection and disability insurance needs consider whether whole of life is appropriate for the following:

### Lifestyle protection

Check if the clients partner/spouse would be vulnerable if the client died, check how long the dependants will rely upon his/her income - consider whether whole of life more effectively addresses client need than term assurance.

### Debt protection

Debts in the short-term and continuing lifestyle protection needs thereafter may be better addressed by whole of life assurance than term assurance.

### Funeral expenses

Most people don't wish to burden their loved ones with the cost of their funeral. If not covered within lifestyle protection, consider whole of life with guaranteed premiums for funeral expenses.

### Inheritance tax mitigation

Check to see if the client's estate is likely to be in excess of the IHT threshold taking into account any monies he/she may inherit themselves. Arrange whole of life plans written in trust to offset any liability.

### Estate protection

Calls on the client's assets in later life, for example, care home fees, reduces the legacy the client can leave to their family and friends. Consider whole of life assurance to replace these liabilities.

### Wealth creation

Many clients want to leave a legacy to their loved ones. Insurance is a tax effective way of creating wealth on death. Premiums out of normal income are not regarded as lifetime gifts for IHT purposes and benefits written in trust can be free of inheritance tax on death.

### Corporate opportunities

Investigate clients' corporate connections - some may be shareholders or partners in firms which have little or no business protection in place. The opportunity may exist to write quality whole of life business to facilitate succession planning and continuity cover.

### Single clients - no dependants

Whilst the client may have no one who is financially dependent on them, this does not mean to say that they will not want to leave money to their family and friends when they die. Once the client's income protection and disability insurance requirements have been addressed, advisers should consider protecting the estate against unpaid debts at the date of death and other expenses that could reduce the estate. Many people do not want to be a burden on their family when they die and at the very least want their funeral to be taken care of - consider a whole of life plan for funeral expenses.



## The product market

Excluding the guaranteed acceptance plans, which are largely marketed direct, there are 15 whole of life assurance products now available in the market from 13 providers; 11 of these are distributed through advisers.

Whole of life product market				
Provider	Product	Type	Cover	Adviser Product
Aviva	Guaranteed Whole of Life Plan	Non profit	Life	Yes
Canada Life International	Flexible Life Plan	Unit linked	Life	Yes
Legal & General	Whole of Life Protection Plan	Non profit	Life	Yes
LV=	LifeTime +	Non profit	Life	Yes
NFU Mutual	Low Cost Whole of Life Policy	Low cost	Life	No
NFU Mutual	Whole of Life	With-profit	Life	No
Partnership	Whole of Life Insurance	Non profit	Life	Yes
PruProtect	PruProtect	Non profit	Life & critical illness cover	Yes
PruProtect	PruProtect Essentials Plan	Low cost	Life & critical illness cover	Yes
Scottish Provident	Pegasus Whole of Life Plan	Non profit	Life	Yes
Scottish Widows	Protection for Life - Lifetime Cover	With-profit	Life	No
Sheffield Mutual Friendly Society	Sheffield Protect Whole of Life Plan	Non profit	Life	Yes
Skandia	Skandia Protect - Guaranteed WOL Plan	Non profit	Life	Yes
Smart Insurance	Smart Life Insurance with Optional Covers	Non profit	Life & critical illness cover	No
Zurich Assurance	Adaptable Life Plan - Guaranteed Payments	Non profit	Life	Yes

Following the withdrawal from the market of the few remaining unit linked whole of life plans in November 2012, those plans remaining are either non-profit or with-profit plans. There is one low cost product: PruProtect's Essentials Plan. Canada Life International has retained the unit linked structure of its Flexible Life Plan for the purposes of costing the cover but the plan itself no longer accrues a maturity value. All products provide a death benefit; PruProtect and Smart Insurance can also include a critical illness benefit.

All these products may be sold under ICOBS and where commission is available it may continue to be taken post-RDR; this would not have been the case with a traditional unit linked whole of life plan.



## Waiver of premium

Having identified that protection is important and having made a suitable recommendation, it is important that inability to pay premiums does not derail clients' financial plans. Waiver of premium benefit is available with nine of the whole of life plans. With the exception of Zurich Assurance, all offer an 'own occupation' definition as a default and most also offer an Activities of Daily Living (ADL) or an Activities of Daily Work (ADW) test where 'own occupation' cannot be offered, as shown in the table below. Scottish Provident's Pegasus plan offers one year own occupation definition for occupations not eligible for full own occupation cover. After a year, the disability definition switches to a serious illness or everyday tasks list. Deferred periods of three or six months are widely available; some plans also have additional flexibility with a range of deferred periods to suit client circumstances.

Waiver of premium terms					
Provider	Product	Definition of Disability	Deferred period	Max Age at Entry	Age Ceases
Canada Life International	Flexible Life Plan	Own	26 weeks	59	64
Legal & General	Whole of Life Protection Plan	Own/ADL	26 weeks	54	60
LV=	LifeTime +	Own/ADW	1/2/3/6 months	59	84
PruProtect	PruProtect	Own	7 days or 1/3/6/12 months	64	75
PruProtect	PruProtect Essentials Plan	Own	7 days or 1/3/6/12 months	64	75
Scottish Provident	Pegasus Whole of Life Plan	Own/Own for one year/serious illness/ADW/ADL	13/26/52 weeks	64	84
Scottish Widows	Protection for Life - Lifetime Cover	Own/Suited/ADW	26 weeks	60	66
Skandia	Skandia Protect - Guaranteed WOL Plan	Own/ADW	6 months	62	64
Zurich Assurance	Adaptable Life Plan - Guaranteed Payments	Suited	3 months	55	65

## Guaranteed Insurability

Eight of the policies include guaranteed insurability options such that cover may be increased if circumstances dictate without the requirement for further medical evidence. With the exception of Skandia, guaranteed insurability is typically only available to standard rate cases. Typically the option must be exercised by age 55 or, in the case of retirement or IHT options, later.

Guaranteed insurability options					
Provider	Product	Max Age	Marriage/ Civil Partner	Childbirth/ Adoption	Mortgage/ Loan increase
Canada Life International	Flexible Life Plan	unlimited	Yes	Yes	Yes
Legal & General	Whole of Life Protection Plan	49/64	Yes	Yes	Yes
LV=	LifeTime +	55/60/64/65/68	Yes	Yes	Yes
PruProtect	PruProtect	54	Yes	Yes	Yes
Scottish Provident	Pegasus Whole of Life Plan	55/69	Yes	Yes	Yes
Skandia	Skandia Protect - Guaranteed WOL Plan	55/65/90/80	Yes	Yes	Yes
Zurich Assurance	Adaptable Life Plan - Guaranteed Payments	54/69	Yes	Yes	Yes
Aviva	Guaranteed Whole of Life Plan	unlimited	No	No	Yes
Canada Life International	Flexible Life Plan	unlimited	No	Yes	Yes
Legal & General	Whole of Life Protection Plan	49/64	No	Yes	Yes
LV=	LifeTime +	55/60/64/65/68	Yes	Yes	Yes
PruProtect	PruProtect	54	No	No	Yes
Scottish Provident	Pegasus Whole of Life Plan	55/69	Yes	Yes	Yes
Skandia	Skandia Protect - Guaranteed WOL Plan	55/65/90/80	Yes	No	Yes
Zurich Assurance	Adaptable Life Plan - Guaranteed Payments	54/69	Yes	Yes	Yes

With IHT mitigation being a major use of whole of life, unsurprisingly, all eight policies offer an IHT increase option; all of these except Aviva also have options triggered by marriage/civil partnership and childbirth/adoption. Such options are suited to lifestyle protection. Five policies (namely those offered by Canada Life International, Legal & General, LV=, Scottish Provident and Zurich) offer guaranteed insurability when business interests increase; such options are suitable for succession planning.

## Ease of acquisition

Making protection easier to buy is a significant challenge for the industry and one it is important to address if more people are to have the cover they need but which may not be high up on their list of wants. The guaranteed acceptance plans for over 50s have been successful in this field with many people purchasing direct with no underwriting being necessary. With intermediated business, customers benefit from an advised sale but having a slick and uncomplicated process is nevertheless desirable from both the client and adviser's perspective.

Most whole of life providers offer access to policy literature online and most operate some form of tele-underwriting or an online application process. Tele-underwriting can remove the burden from advisers and reduce the risk of non-disclosure for clients and advisers. Increasingly sophisticated online submission processes too can save time by reducing administration resulting in reduced costs for advisers and a quick underwriting decision in many cases.

Ease of acquisition			
Provider	Product	Online Literature	Underwriting Process <sup>7</sup>
Aviva	Guaranteed Whole of Life Plan	Yes	Little †
Canada Life International	Flexible Life Plan	Yes	Little †
Legal & General	Whole of Life Protection Plan	No	Big T
LV=	LifeTime +	Yes	Big T
NFU Mutual	Low Cost Whole of Life Policy	No	Big T
NFU Mutual	Whole of Life	No	Big T
Partnership	Whole of Life Insurance	No	Paper based
PruProtect	PruProtect	Yes	Online & little †
PruProtect	PruProtect Essentials Plan	Yes	Online & little †

<sup>7</sup> Big T tele-underwriting - the applicant completes basic information and all health and lifestyle information is collected via a telephone interviewer leading to an underwriting decision.

Little † tele-underwriting- comprises a traditional application with a health and lifestyle questionnaire in paper form or an online application followed up by a tele-interview where further information is required.



## Ease of acquisition (continued)

Provider	Product	Online Literature	Underwriting Process
Scottish Provident	Pegasus Whole of Life Plan	Yes	Online & little †
Scottish Widows	Protection for Life - Lifetime Cover	Yes	Online
Sheffield Mutual Friendly Society	Sheffield Protect Whole of Life Plan	Yes	Paper based
Skandia	Skandia Protect - Guaranteed WOL Plan	Yes	Big T
Smart Insurance	Smart Life Insurance with Optional Covers	Yes	Online submission
Zurich Assurance	Adaptable Life Plan - Guaranteed Payments	Yes	Online & little †



## Premiums

The way that premiums are calculated and paid is a distinguishing feature of the various types of whole of life assurance. While cover continues for the remaining life of the assured, the premiums do not necessarily have to continue to be paid beyond a specified point. However, cover may have to decrease if the cost of the underlying risk is not met.

All plans except those offered by Canada Life International and Smart Insurance have guaranteed premium rates.

With guaranteed rates the premiums are agreed at outset and do not increase unless there is a one-off increase in the sum assured or an automatic increase option is chosen. Reviewable rate contracts are established with a regular premium which holds good for typically 10 years, after which it has the potential to increase to take account of the higher costs of cover due to increased age of the lives assured.

For maximum cover plans, Canada Life International reviews premiums after 10 years, whatever the age of the life assured when the plan starts, and every five years thereafter. For other cover levels, if the client is aged 61 or over when the plan starts, the first review will be after five years. If the client reaches the age 110 the plan will be reviewed yearly.

With Smart Insurance's plan, the premium and benefit amounts increase each year. The new premium takes account of the client's age and the benefit amount increase if the client chooses to accept the increase in cover.

Many clients value the certainty that guaranteed rates gives; however, affordability may be an issue. Reviewable rates are a cost effective way of arranging cover particularly if the need for life assurance becomes less critical later in life.

PruProtect and Scottish Provident offer a choice of guaranteed or reviewable rate contracts.

Scottish Provident offers cover on a standard, guaranteed premium basis or maximum, reviewable premium basis.

The maximum basis provides the highest level of cover for the lowest initial premium. Premiums are reviewed after 10 years and every five years thereafter.

Where reviewable rates are chosen, PruProtect undertakes a review on the tenth plan anniversary or when the insured life reaches age 70 (age 75 for Serious Illness Cover) if earlier. If there is a change of premium the next review is undertaken after another 10 years otherwise subsequent reviews occur annually.

## Appendix - Potential IHT charges

When assets are placed in a discretionary trust, if they exceed the IHT threshold, there is a charge of 20%. This could affect existing whole of life policies that are placed in trust now because many traditional whole of life policies accrued an investment element and the charge is calculated with reference to the surrender value of the policy (or the premiums paid, if greater). In cases where an existing policy is placed in trust and the donor is seriously ill, the value of the gift is deemed to be the value of the sum assured.

New whole of life policies are unlikely to be affected; the premiums in the first year will most likely be below the annual exemption of £3,000 or will be classed as exempt gifts for the IHT purposes because they are part of everyday spending.

There is a periodic charge levied on each tenth anniversary of the trust. This is up to 6% of the value of the assets over the nil rate band. This may affect traditional policies with a surrender value; new policies such as the Pegasus plan however have no surrender value and would only incur a periodic charge if the premiums paid in were so large compared to disposable income that they were deemed not to be normal expenditure.

A proportionate, exit charge may apply where assets are distributed to the beneficiaries in between the 10 year anniversaries. Typically, a proportionate charge will not apply unless the assets are held in the trust for a period of time after the claim and are paid out following the first or subsequent 10 year anniversaries.

Typically most protection plans placed in a discretionary trust will not incur an IHT charge but attention should be paid to specific circumstances. Insurers such as Scottish Provident can provide help and support when setting up trusts and have trust document templates for advisers to use with their clients.

If there is the prospect of incurring a periodic or proportionate charge of 6%, it may still be preferable to use a discretionary trust to avoid the greater 40% charge that may be levied on the estate. Alternatively, if the client does not require the flexibility of a discretionary trust, advisers can consider using a bare trust instead and avoid any IHT charges.

## What have we learned?

### Questions

#### Question 1

Removing the investment element from whole of life policies has opened up an opportunity for advisers. Which of the following best describes why?

- A. Both ICOB and COB-registered advisers can recommend whole of life assurance.
- B. Whole of life assurance is most suitable for a restricted panel.
- C. Previously, whole of life assurance was only sold direct.
- D. Whole of life is suitable for estate planning, business protection and lifestyle protection.

#### Question 2

For which of the following scenarios is a whole of life assurance recommendation least suitable?

- A. Mrs. Price is retired and has no financial dependants, her estate is not large and she wants to avoid burdening her relatives with costly funeral expenses on her death.
- B. A young couple has a 25 year mortgage and need a cost effective solution to protect the debt.
- C. Mr. Smith and Mrs. Smith are retired; Mr. Smith has a single life annuity with no widow's benefits.
- D. Mr. and Mrs. Jones are in their fifties and have nine years left on their mortgage and no protection in place.

#### Question 3

For which of the following business protection scenarios is a whole of life assurance likely to be least suitable?

- A. The managing director of ABC Ltd is the guarantor for a £200,000 business loan repayable in eight years' time.
- B. A controlling shareholder in a limited company is considering retirement in the next 10 years but intends to retain his interest and keep working part time. His wife and children have no experience or interest in the firm.
- C. The Sales Director of a firm accounts for 75% of the revenue.
- D. Two partners in a business have no plans to sell up and retire while they can still work but have no contingency in place should one of them die.

#### Question 4

An underwritten whole of life assurance plan has certain advantages over a guaranteed acceptance plan; which of the following are true?

- A. For clients in good health, an underwritten policy is always better value for money.
- B. Underwritten whole of life assurance pays out on death whenever it occurs.
- C. Guaranteed acceptance plans are mainly for paying funeral expenses
- D. Underwritten whole of life assurance pays out on critical illness as well as on death.

#### Question 5

Which of the following financial planning scenarios present an opportunity for non-profit whole of life assurance? Note - there may be more than one correct answer.

- A. Mr. and Mrs. Smith have a large combined estate; they want to pass it on to their children tax efficiently.
- B. Mr. and Mrs. Jones have children in private school for the next 15 years; they want to protect their earnings in the case of their premature death so the school fees can continue to be paid.
- C. Mrs. Gray is approaching retirement but has few savings. She would like to pass a legacy to her grandchildren when she dies.
- D. Mr. White is concerned about long-term care costs and the effect they might have on his hard earned savings; he wants his children to benefit fully from his estate when he dies.

## Answers

### Question 1 - The correct answer is A

- A. RDR has introduced adviser charging for investment contracts; non-profit whole of life falls outside this category meaning it can be sold by both ICOB and COB-registered advisers.
- B. Whole of life assurance should be considered in the context of a whole of market proposition and can be part of a restricted panel but isn't exclusive to either.
- C. Much whole of life assurance is sold direct in the form of guaranteed acceptance plans but underwritten plans have always been available through the intermediated channel.
- D. Whole of life has always been suitable for these financial planning scenarios and remains so.

### Question 2 - The correct answer is B

- A. Whole of life assurance is suitable for providing cover for funeral expenses when Mrs. Price dies; any benefits left over can be passed to her children or grandchildren as a legacy.
- B. In order to protect a 25 year liability with whole of life assurance it would be necessary to select guaranteed rates, which may prove costly compared with simple term assurance.
- C. Whole of life assurance can be used to insure Mrs. Smith against the loss of Mr. Smith's pension on his death.
- D. A reviewable whole of life policy will typically not increase premiums or decrease benefits in the first 10 years and is therefore a cost effective option; thereafter the policy can be used for lifestyle protection with the Joneses choosing to increase the premiums to maintain cover.

### Question 3 - The correct answer is C

- A. ABC Ltd is at risk if the managing director dies within the next eight years and whole of life assurance may be a cost effective solution, and useful if there are continuing protection needs after the loan is paid off. Term assurance should also be considered.
- B. It is important that the firm has the funds to purchase the shares when the controlling share-holder dies whenever that may occur and whole of life can meet this need.
- C. The firm's revenues are at risk if the sales person dies but absence due to disability or sickness is more likely. Consider key person income protection insurance.
- D. When there is no definite date for winding up the business, whole of life is good to protect against one of the partners dying. Each partner writes a policy on the life of the other enabling them to purchase their share of the business should the other die.



#### Question 4 - The correct answer is B

- A. While it is true underwritten policies generally secure greater benefits than guaranteed acceptance plans, much will depend on how long the client holds the policy and the sustainability of premiums.
- B. Typically, guaranteed acceptance plans will exclude death by natural causes in the first two years of a policy. The underwritten policy has no such moratorium.
- C. The proceeds from a guaranteed acceptance plan can be used for any purpose as can the proceeds from an underwritten plan. Some policies are marketed specifically for funeral expenses.
- D. Some policies can include critical illness benefits but this is not a common feature of whole of life assurance today.

#### Question 5 - A, C and D are correct

- A. Whole of life is eminently suitable for inheritance tax planning providing the correct trust advice is given.
- B. For certainty of cover, fixed term liabilities in excess of 10 years are best protected by term assurance because guaranteed premium whole of life could prove more expensive. Terms up to 10 years can be insured on a maximum cover basis pending the first premium review.
- C. Whole of life assurance can be used to create wealth for dependants.
- D. Expenses in later life such as long-term care can eat into the estate. A whole of life assurance can replace these assets.

A word from our sponsor

*"I want  
to protect  
my family"*

Use a whole of life  
plan to provide financial  
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PROTECTION  
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