THE FLEXIBILITY OF SEGMENTATION

THIS GUIDE OUTLINES THE GENERAL BENEFITS/ADVANTAGES OF USING A PLAN THAT HAS MULTIPLE SEGMENTS COMPARED TO ONE THAT DOES NOT.

WHAT IS A SEGMENT?

Where a Life Assurance or Capital Redemption plan/policy is issued with sub-plans/policies, these are known as individual segments.

HOW DO I KNOW IF THE PLAN IS SEGMENTED?

You can usually tell from the plan number. The number of segments should be shown on the plan schedule after the specific reference number allocated to it, for example:

CL10001234 (1-100): This particular plan has 100 segments

CL10004321 has no segments.

The main benefits of segmentation centre around simplifying how payments from plan are taxed and providing flexibility in respect of transferring funds to others.

The following examples illustrate the most popular uses of segmentation:

EXAMPLE 1: TAXATION OF THE PLAN

How the plan is taxed depends on the jurisdiction that the owner is tax resident in. Whilst the UK has a 5% tax deferred allowance, this isn't the case in any other country and so more often than not a complex tax calculation is required to ascertain what part of the withdrawal is income/growth and what part is capital. Going forward, rebasing calculations are usually required to factor in previous withdrawals and gains.

With a segmented plan it's so straightforward, as you only have to work out the gain on the segments being cashed in.

Example

Plan funded with a single payment of £250,000 and the plan owner requires an amount of £85,000. The current value of the plan is now £325,000. The plan was issued with 100 segments.

- Each plan segment initial value: **£2,500** (£250,000/100)
- Current value of plan each segment: **£3,250** (£325,000/100)
- 27 segments surrendered will provide **£87,750** (£3,250 * 27)
- Gain per segment = **£750** (£3,250 - £2,500)

No rebasing of the plan is required. The gain is based on (current value/number of remaining plan segments) less (original value/number of remaining plan segments). Segmentation is also really useful where UK residents require more than their accumulated 5% tax deferred allowance.

EXAMPLE 2 – TRANSFERRING PLAN BENEFITS TO OTHERS

The plan is owned jointly and the owners are recently divorced. The plan must be divided 50/50.

- With a plan issued with 100 segments, 50 segments could be assigned to each party.
- Each party would have their own individual plan going forward.
- Both plans will have their own set of standard and establishment fees.
- No requirement for the investment to be liquidated to cash. Both individuals can remain invested in the market.

If the plan was not segmented then either the plan would have to be surrendered or a withdrawal taken to pay out one of the owners followed by an assignment.

- A withdrawal would require a decision to be made as to which party receives cash/remains in control of the plan.
- The party retaining control of the plan would be subject to all the charges
- Reinvestment of cash into new investment could have additional costs as well as loss in performance from being out of the market.
- Depending on the assets of the plan, it may not be possible to take withdrawal at that point in time.

Segmentation offers a lot of options/flexibility here.

EXAMPLE 3: TAX PLANNING

The plan owner is looking to release funds from the plan to fund a university trip for a child.

Segments can be gifted to the child (aged 18+) who can then surrender in their own name. This means that any tax liability on the surrender of those segments should then move from the original owner to the child. The child could be a lower or non-taxpaying individual.

If the plan was not segmented, then a withdrawal would have to be taken which could result in a tax liability for the owner, even though they are passing on the funds to someone else.

IMPORTANT NOTES

It is not possible to transfer/surrender part of a plan segment. It may therefore be necessary to surrender an additional plan segment to achieve the required income amount.

Please note that every care has been taken to ensure that the information provided is correct and in accordance with our understanding of law and HM Revenue and Customs' (HMRC) practice.

You should note however, that we cannot take on the role of an individual taxation adviser and independent confirmation should be obtained before acting or refraining from acting upon the information given. The law and HMRC practice are subject to change.

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