Briefing Note 27

This Briefing Note is based on a Newsletter issued by Foden Baynes Associates in September 2006. We gratefully acknowledge their permission to make use of their information.

Death Benefits under small money purchase schemes and the new Post A-Day legislation

This briefing note is intended as a guide to the impact on Death Benefits under the new legislation.

Timing of Lump Sum Death Benefit Payment

Scheme administrators must pay any lump sum death benefits within two years of death. If the death is not advised to them within this period a tax charge of 40% will be applied and deducted from the lump sum.

More than one Dependant

It is possible to leave funds to more than one dependant upon death. In this case funds would be allocated between each dependant by the scheme Trustees following the instruction as indicated in the member's expression of wish.

Member dies prior to taking benefits

If a member dies prior to any Benefit Crystallisation Event the full value of the fund up to the Standard Lifetime Allowance (SLA) or Personal Lifetime Allowance (PLA) (in the case of enhanced/primary protection), can be paid to a nominated beneficiary as a tax-free lump sum. Any amount in excess of the SLA/PLA can be paid as a lump sum subject to a 55% tax charge.

Recent clarifications from HMRC have indicated that any lump sum death benefits paid on death before age 75 will normally be free of Inheritance Tax. This is the formulisation of the concessionary practice operated by HMRC.

Alternatively, funds can provide a taxable dependants pension, as follows:

- Dependants' secured annuity, purchased with any recognised annuity provider.
- Dependants' unsecured pension and/or Short Term annuity contract(s) where the dependant is under age 75.
- Dependants' alternatively secured pension when the dependant is aged 75 or over.

There will be no test against the lifetime allowance where the death benefits are paid as dependants' pensions.

The amount of dependents' unsecured pension will be based on special GAD rates applicable to the dependant's age and will be reviewed every year. The maximum will be 120% of the base amount.

In the case of dependants' alternatively secured pension the amount will be calculated by special GAD tables rates applicable to age 75 and reviewed every year. The maximum will be 70% of the basis amount.

Short-term annuity contracts cannot exceed 5 years in term and must cease prior to the date on which the dependant reaches age 75.

The commencement date of dependant pension will be from the time the dependant is entitled to the benefit and not the date the member died. It is not possible to have a guarantee period.

Member dies prior to age 75 while in receipt of Unsecured Pension

Under the above circumstance the following benefits may be provided:

- Return of balance fund less a 35% tax charge. There is no time restriction on payment, so long as reasonable.
- Secured annuity for dependant.
- Unsecured pension for dependant under age 75 and/or short-term annuity contract(s).
- Alternatively secured pension for a dependant over age 75.

Member dies after 75 while in receipt of Alternatively Secured Pension

Under the circumstance the following benefits may be provided to a dependant:

- Secured annuity for dependant
- Unsecured pension for dependant under age 75 and/or short term annuity contract(s)
- Alternatively secured pension for a dependant over age 75.

If there is no surviving dependant the remaining funds can be paid to either:

- A charity nominated by the member

or

- Transferred to the pension fund of another member of the same arrangement as a transfer lump sum death benefit.

Death of a dependant before 75 while in receipt of Unsecured Pension

Under the above circumstance the following benefits may be provided:

- The dependants' estate may elect to pay a 35% tax charge on the remaining fund and have the balance paid out as a lump sum. There is no prescribed time scale for this to happen as long as it is reasonable and/or;
- Other surviving dependants' of the original deceased member may receive additional funds from the deceased dependants' arrangement.

Dependant reaches age 75 while in receipt of Unsecured Pension

When a dependant reaches age 75 the unsecured pension converts to alternatively secured pension. The amount of pension will be recalculated on the alternatively secured pension basis. This will then be reviewed annually.

The dependant may elect to use the balance funds to purchase a secured annuity instead

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Death of a dependant while in receipt of alternatively Secured Pension

If there are other surviving dependants of the original deceased member any remaining dependants' alternatively secured pension fund may be used to provide:

- Unsecured or alternatively secured pension depending on the surviving dependants' age.
- Alternatively, if there are no surviving dependant's then this can be paid as a charity lump sum benefit.
- Or a transfer lump sum death benefits.

Disclaimer

All of the information contained within this newsletter is based on WFW current understanding of the current legislation as defined by HMRC. This information should be used as a guide only and in no way over-rides HMRC requirements as outlined in the Registered Pension Schemes Manual and other Legislation.
These notes are based on a newsletter from Foden Baynes Associates Limited; we gratefully acknowledge their permission to use it. E & O Excepted

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