

Death Benefits

This leaflet explains

- The effect of legislation on the payment of death benefits
- Possible tax liability for anyone receiving death benefits (whether paid as a lump sum or used to provide income by buying an annuity or designating to drawdown), and

- The responsibilities for **Personal Representatives**.

A **Personal Representative**, in relation to a person who has died, is responsible for administering the estate of the deceased.

Death Benefits

This leaflet covers the position on death before age 75 where there is an uncrystallised death benefit. An uncrystallised death benefit arises where death has happened before the pension fund has been put in to payment for the member.

Note: Different rules apply on death after age 75, and these are not covered in this leaflet.

Death benefit payments

From 6 April 2006, the Government introduced an overall Lifetime Allowance. This is set at £1,073,100 for the 2022/23 tax year. Protection may be available (or may already have been applied for and granted by HMRC) for those with benefits that may exceed the Lifetime Allowance.

There may be a Lifetime Allowance Charge (a tax charge, where death benefits from pension plans exceed the deceased person's available Lifetime Allowance), on any excess of the total death benefits from pension plans over the deceased person's available Lifetime Allowance.

Two year timescale

There will be tax implications where death benefits are not paid within two years of the earlier of,

- The day the Scheme Administrator first knew of the death; and
- The day the Scheme Administrator could first reasonably have been expected to know of the death.

Death Benefits over the Lifetime Allowance

Importance of this leaflet

Anyone receiving a death benefit from a pension plan (a beneficiary) will have some tax to pay if the total death benefits are over the available Lifetime Allowance.

If you are a Personal Representative, you have special additional responsibilities to report payments over the available Lifetime Allowance to HMRC.

In practice, the Lifetime Allowance tax charge will not often apply.

If you think a Lifetime Allowance Charge may apply, you should read this leaflet.

Questions & answers for personal representatives

Q. Why is there a tax charge on death benefits paid from pension funds?

A. The Government changed the rules on the benefits that can be paid from pension schemes from 6 April 2006. Where the total death benefits payable from pension plans are over the available Lifetime Allowance, there will be a tax charge. In practice, this tax should not affect many people.

The value over the Lifetime Allowance is called the chargeable amount. Where this is paid as a lump sum within two years of notification of the client's death, a tax charge of 55% on the chargeable amount will apply, called a Lifetime Allowance Charge.

Any chargeable amount used to provide pension income for a dependant or nominee of the deceased, will be subject to a tax charge of 25%. So tax may be reduced by choosing the income option for some/all of the chargeable amount. Assuming the deceased was under age 75 at the date of death, any income will be paid tax free.

Where benefits are not paid within two years of notification, no Lifetime Allowance Charge will apply. See further details in this leaflet of the tax applicable.

Q. What about Inheritance Tax?

A. Pension funds do not normally attract Inheritance Tax.

However, Inheritance Tax may apply where the scheme administrator has no discretion on who benefits are paid to on death.

Also, it could apply where someone who is expected to live less than two years:

- alters the term of their pension contract, or
- makes unusually large contributions, or
- assigns benefits into trust
- transfers benefits from one scheme to another

Inheritance Tax and Pensions is a complicated area and independent advice from a solicitor, tax or financial adviser is recommended if you believe Inheritance Tax may apply.

Q. Could Inheritance Tax and the Lifetime Allowance Charge both apply?

A. Yes – in exceptional circumstances, if a lump sum payment forms part of a deceased's estate and a Lifetime Allowance Charge applies.

Q. Are there any other tax charges?

A. If benefits are not paid within two years of notification of death (as referred to earlier in this leaflet), these will be subject to tax.

If the death benefit is used to buy an annuity or is designated to drawdown, income taken will be subject to the recipient's marginal rate of tax.

If paid as "an Uncrystallised Funds Lump Sum Death Benefit" after 5 April 2016, payments will generally be subject instead to the recipient's marginal rate of tax, but see below.

The tax the Scheme Administrator will deduct from this lump sum may differ if it is to be paid to a "non qualifying person" i.e. the person is not an individual, or they are an individual and the payment is made to them in their capacity as a trustee, a personal representative, a director of a company, a partner in a firm or a member of a limited liability partnership. Please contact us for more information if this is the case.

Questions and answers for those who receive a death benefit

Q. Will I have to pay any tax?

A. Yes, where a Lifetime Allowance Charge applies, each person who is allocated any pension death benefit is responsible for his/her share of the tax on the total benefit over the Lifetime Allowance. If you are allocated the whole death benefit, you are responsible for the full tax charge. If you share the benefits, say you get half, you are responsible for half the tax charge.

Any death benefits not settled within the two year timescale (see page 1 for further details) will not be subject to the Lifetime Allowance Charge, however, the recipient will pay income tax at their marginal rate on payments received.

There may also be, in exceptional circumstances, a liability for Inheritance Tax.

Q. How will I know if a Lifetime Allowance Charge is due?

A. The Personal Representatives are responsible for working this out and notifying HMRC.

HMRC has six years from the date they are told about the chargeable amount to claim the tax from beneficiaries.

If there is tax to pay, HMRC will expect payment within 30 days of the request for payment.

Q. Will Prudential be able to tell me if there is a Lifetime Allowance Charge?

A. No. HMRC rules mean the responsibility for this lies with the Personal Representatives. In any event, there could be benefits from plans elsewhere, which Prudential has no knowledge of."

Q. Why is it the beneficiaries who pay the tax?

A. The Government decided that, if tax is due, each person receiving death benefits must pay the appropriate share of the tax due.

Questions & answers for personal representatives

Q. Are we responsible for paying the Lifetime Allowance Tax Charge?

A. No, the people who receive death benefits from the pension plans have to pay the tax.

Q. What are our responsibilities?

- A.
- Gather enough information about the deceased's pension funds to work out if there is a Lifetime Allowance Charge.
 - Work out the value of the Lifetime Allowance Charge.
 - Where there is a Lifetime Allowance Charge, send details to HMRC.

Q. Where will I get the information to check for a liability for a Lifetime Allowance charge?

A. You'll get details from the pension provider/scheme that was paying the pension to the deceased and that paid any death benefits. The deceased's personal papers may also help.

Q. Will I need special authority to get information about the pension funds.

A. No, registered pension schemes and pension providers must give Personal Representatives information about the deceased's pension plans to work out if any tax is due.

The scheme or company will need to be satisfied that you are the Personal Representative.

Q. What benefits need to be taken into account?

A. **Death benefits:** The total value of uncrystallised death benefits payments from registered pension schemes, including individual pension plans.

Pension/lump sum benefits crystallised prior to date of death:

Any amounts already vested/crystallised e.g lump sums, annuities, drawdown arrangements must be taken into account.

Q. Are any benefits excluded?

A. State pensions and any pension being paid to the deceased as a result of someone else's death should be ignored.

Any benefits paid as unauthorised payments are excluded from the total value of benefits paid.

Any death benefit lump sums or income payable from plans already crystallised e.g drawdown arrangements, scheme pensions, annuities.

The Lifetime Allowance test can be complex. If you think benefits could exceed the Lifetime Allowance, you may wish to seek specialist financial advice and/or refer to gov.uk/hmrc

Q. Is the Lifetime Allowance the same for everyone?

A. No, some people may have applied to HM Revenue and Customs for transitional protection to protect their benefits from a Lifetime Allowance Charge. A few people may have later adjustments to their Lifetime Allowance after 5 April 2006 or may not be entitled to the full Lifetime Allowance.

Q. How will we know if benefits have been protected?

A. The deceased should have a certificate from HMRC if protection applies. You could contact HMRC and ask them if you are uncertain whether protection applies.

Q. If there is a chargeable amount, what happens?

- A. You will need to give the following details to HMRC:
- The name of the registered pension scheme or individual plan that paid the death benefits
 - The scheme administrator's name and address
 - The deceased member's name and National Insurance number
 - The amount(s) and date(s) of payments under each scheme/plan.
 - The chargeable amount. i.e the value of the death benefits over the Lifetime Allowance.

Questions & answers for personal representatives continued

Q. When do we need to inform HMRC and how do we do this?

- A. Personal Representatives should provide the information about the chargeable amount to HMRC within:
- 13 months of the death or, if later,
 - Within 30 days of becoming aware that there is a chargeable amount.

HMRC guidance says that, where the requirement to provide the information arises later, the reporting period is extended to 30 months starting with the date of death. Where Personal Representatives do not discover the relevant information until more than 30 months after the death, the period for reporting is extended to three months following the discovery of the information. There will be penalties for late reporting.

You should give HMRC these details, in writing, to:

**Pension Schemes Services
HM Revenue & Customs
BX9 1GH**

Q. What happens after we've given the details to HMRC?

- A. HMRC will get details of the beneficiaries from all the schemes/providers concerned and then work out how much tax is due from each beneficiary.

HMRC will then contact the beneficiaries to arrange for payment of the tax.

Further information

You may want to speak to a solicitor or financial adviser to guide you through the process.

There is information on the general responsibilities of personal representatives on the HMRC website [gov.uk](https://www.gov.uk)

Information on the pension rules can also be found on the HMRC website.

This leaflet is based on our current understanding as at April 2022 of current taxation legislation and HM Revenue & Customs practice, all of which are liable to change without notice. The impact of taxation (and any tax reliefs) depends on individual circumstances. It is not intended to provide legal advice and we recommend that readers obtain specific legal advice before taking any action.