M&G wealth

Pensions, death and tax

where we've been, where we are, where we're going.

The information that follows is based on our understanding of current taxation, legislation and HM Revenue & Customs practice all of which are liable to change without notice.

This is just for UK financial advice professionals.

Learning Objectives

By the end of this session, you will be able to:

- Describe the tax treatment of pension schemes on death
- Explain the key elements of creating an IHT plan
- Evaluate potential solutions for individuals whose pensions may be caught up in the IHT net




Where we've been...

2011

"Age 75" goes

35% / 45% / 55%

2015

Nominees / Successors Introduced

S3(3) repealed

2011/2014

Vested v Unvested

2023

LTA abolished

Pre 75 v Post 75

Where we are until 2027

AGE 75

NO
IHT
(normally)

NO
IHT
(normally)

NO
INCOME
TAX*

The "2 year" rule

INCOME
TAX
(Marginal / 45%)

* DB income is taxable

Where we're going

AGE 75

~~NO~~
IHT
(normally)

~~NO~~
IHT
(normally)

NO
INCOME
TAX*

The "2 year" rule

INCOME
TAX
(Marginal / 45%)

* DB income is taxable

Both taxes will apply

IHT on pension schemes

Beneficially Entitled	General power of disposal	New rules
Estate entitled	Power of Disposal (with some exceptions)	Discretionary Disposal
Within estate	Within estate	~~Outside estate~~
		Within estate

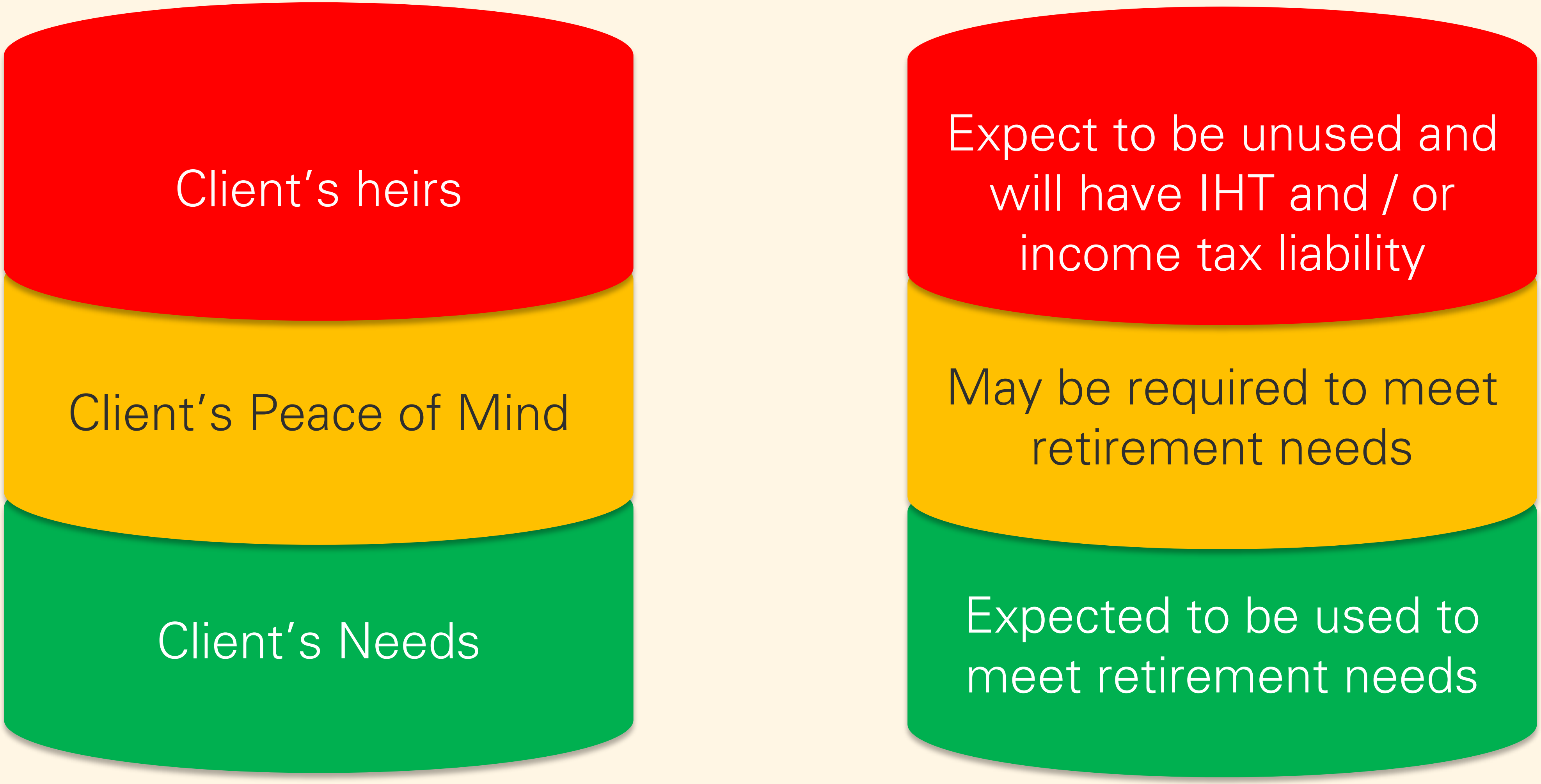
Distribution Arrangements Unchanged

At Autumn Budget 2024, the government announced several measures to reform Inheritance Tax. This included a measure to bring most unused pension funds and death benefits within the value of a person's estate for Inheritance Tax purposes from 6 April 2027.

As part of these changes, pension scheme administrators (PSAs) will become liable for reporting and paying any Inheritance Tax due on unused pension funds and death benefits.

Technical consultation - Inheritance Tax on pensions: liability, reporting and payment, 30TH October 2024

Segmenting pensions



Consultation matters

Rumsfelding

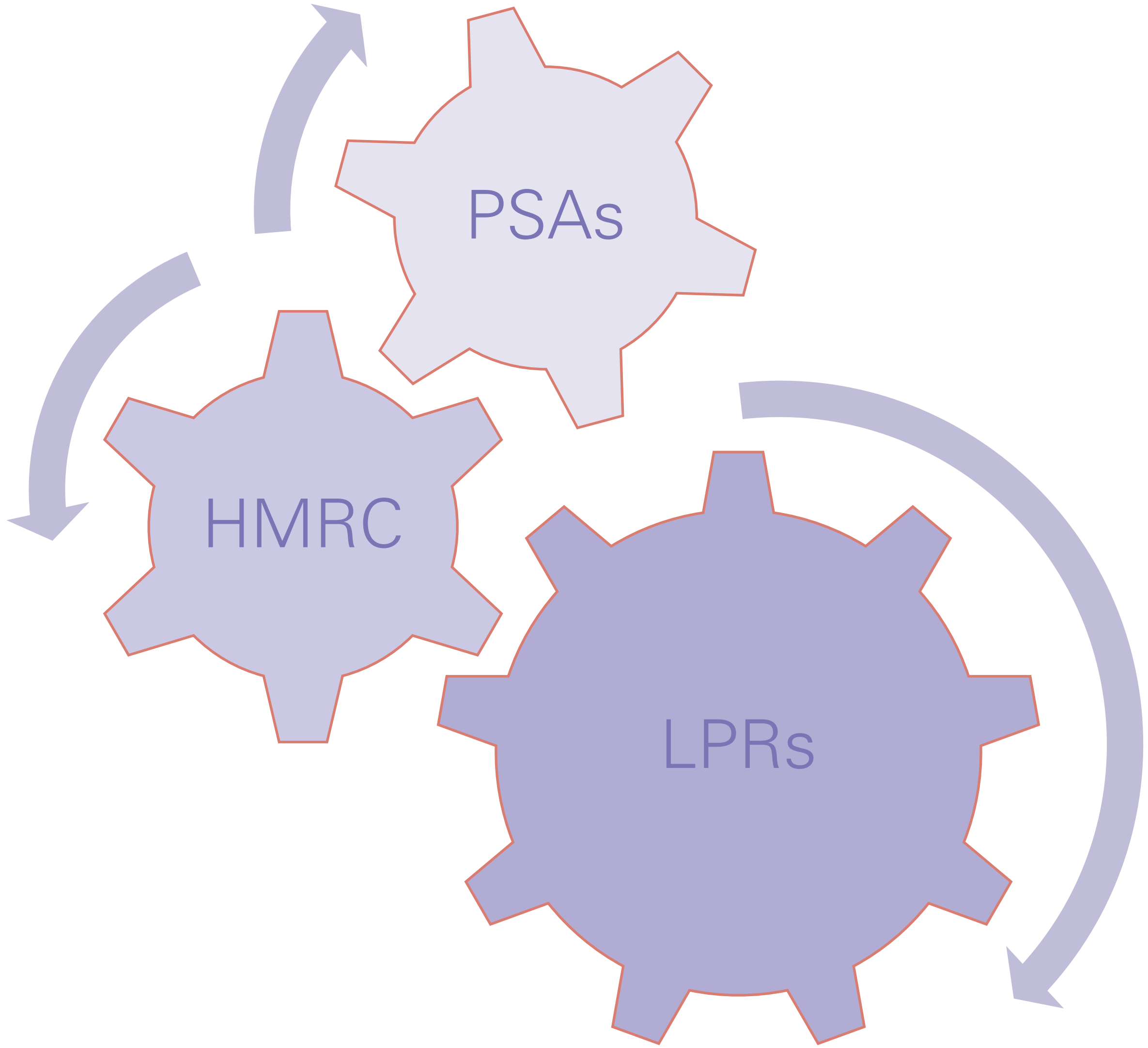
SCOPE OF CHARGE TO IHT

NO CONSULTATION

COLLECTION OF IHT CHARGE

CONSULTATION

Issues, in a nutshell



No pension / non pension estate interaction

"You must pay Inheritance Tax by the end of the sixth month after the person died."
HMRC

Amend deadlines / payment on account

Annuities

Single life

Joint Life
spouse/civil partner

Joint Life
non spouse/civil partner

Guarantee period
Discretionary “disposal”

Value Protection Lump Sums
Discretionary “disposal”

Guarantee period
Estate “disposal”

Value Protection Lump Sums
Estate “disposal”

Remember there’s no annuity in a Fixed Term Annuity

“Risk Benefits”

All life policy products purchased with pension funds or alongside them as part of a pension package offered by an employer are not in scope of the changes in this consultation document.

HMRC consultation

“Risk Benefits” examples

Personal Pensions	Money Purchase OPS	Defined Benefit OPS
Term Assurance £50,000	Death in service £50,000	Death in Service £95,000
Return of Fund £50,000	Return of Fund £50,000	Return of Contributions £5,000

Pensions – IHT events

Annuity guarantees

Pension changes

(incl death benefit changes)

Contributions in Ill-health

Transfers

QSR?
APR?
BPR?

The "2 year" rule?

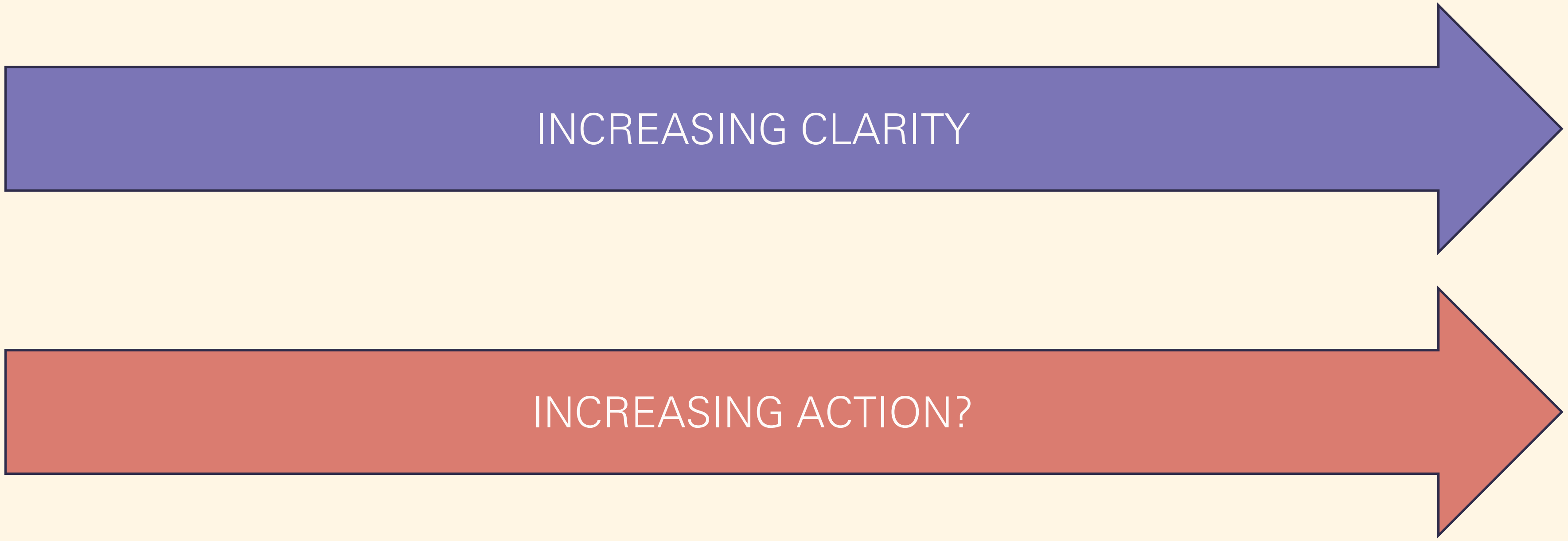
How do these fit in if pension ALSO subject to IHT on death?

Ready, steady, wait…?

22nd Jan 2025

Next:
Consultation response
Technical Consultation on draft legislation

5 April 2027



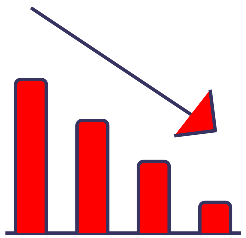
The end will be the same –
it's just the means that may change

Subject to "tax rules might change"

But what if they die before April 2027 and/or before age 75?

Planning matters

Does it matter?



ACCEPT

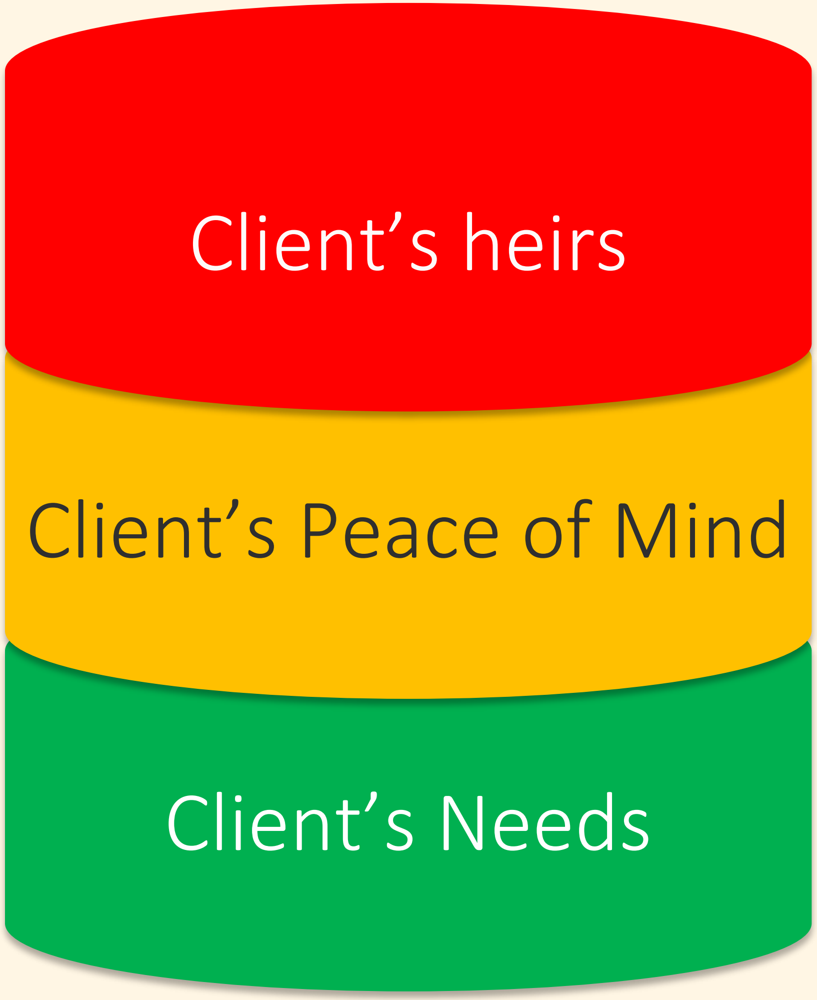
INSURE

PLAN

Continue funding?

Fund beyond here?

What's better?



Probably less tax efficient overall

Venture Capital Schemes:
- 30% income tax relief?
- Business Relief?

Direct to the next generation:
- Access
- Control

Beneficiary's own pension?

LSA/LSDBA Modeller

Inputs

Assumptions & Values

Net fund growth 6%

Age at start 70

LSA

LSDB

RESET ALL

Summary

Assumptions & Values

Net fund growth	6%
Age at start	70

Available Allowances

LSA	£268,275
LSDBA	£1,073,100

Current Fund Values

Unvested	£500,000
Post April 2024 drawdown	£0
Pre April 2024 drawdown	£0

Position at Age	86
Fund Values	
Unvested	£0
Post 24	£952,632
Pre 24	£0
Total tax free	£125,000
Total income	£0
LSA remaining	£143,275
"Ballpark" Contribution required to fully use LSA	£21,060
Lump Sum Death Benefit value	
Unvested	£0
Post 24	£952,632
Total	£952,632
LSDBA remaining	£948,100
Excess	£4,532
Unvested Pot target value	£0
"Ballpark" Benefits to match target value (UFPLS)	£0
Post April 24 pot target value	£0
Income to match target value	£35,007
Excess if target pots met	£0

Available Allowances			Fund	…rawdown	Allowances Used Elsewhere	
Age	LSA	LSDBA	(Start of Y	Income	LSA	LSDBA
70	£268,275	£1,073,100	£500,0	£0	£0	£0
71	£143,275	£948,100	£0	£0	£0	£0
72	£143,275	£948,100	£0	£0	£0	£0
73	£143,275	£948,100	£0	£0	£0	£0
74	£143,275	£948,100	£0	£0	£0	£0
75	£143,275	£948,100	£0	£0	£0	£0
76	£143,275	£948,100	£0	£0	£0	£0
77	£143,275	£948,100	£0	£0	£0	£0
78	£143,275	£948,100	£0	£0	£0	£0
79	£143,275	£948,100	£0	£0	£0	£0
80	£143,275	£948,100	£0	£0	£0	£0
81	£143,275	£948,100	£0	£0	£0	£0
82	£143,275	£948,100	£0	£0	£0	£0
83	£143,275	£948,100	£0	£0	£0	£0
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85	£143,275	£948,100	£0	£0	£0	£0
86	£143,275	£948,100	£0	£0	£0	£0
87	£143,275	£948,100	£0	£0	£0	£0
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94	£143,275	£948,100	£0	£0	£0	£0
95	£143,275	£948,100	£0	£0	£0	£0
96	£143,275	£948,100	£0	£0	£0	£0
97	£143,275	£948,100	£0	£0	£0	£0
98	£143,275	£948,100	£0	£0	£0	£0
99	£143,275	£948,100	£0	£0	£0	£0
100	£143,275	£948,100	£0	£0	£0	£0
101	£143,275	£948,100	£0	£0	£0	£0
102	£143,275	£948,100	£0	£0	£0	£0
103	£143,275	£948,100	£0	£0	£0	£0

PENSION

40% world
IHT

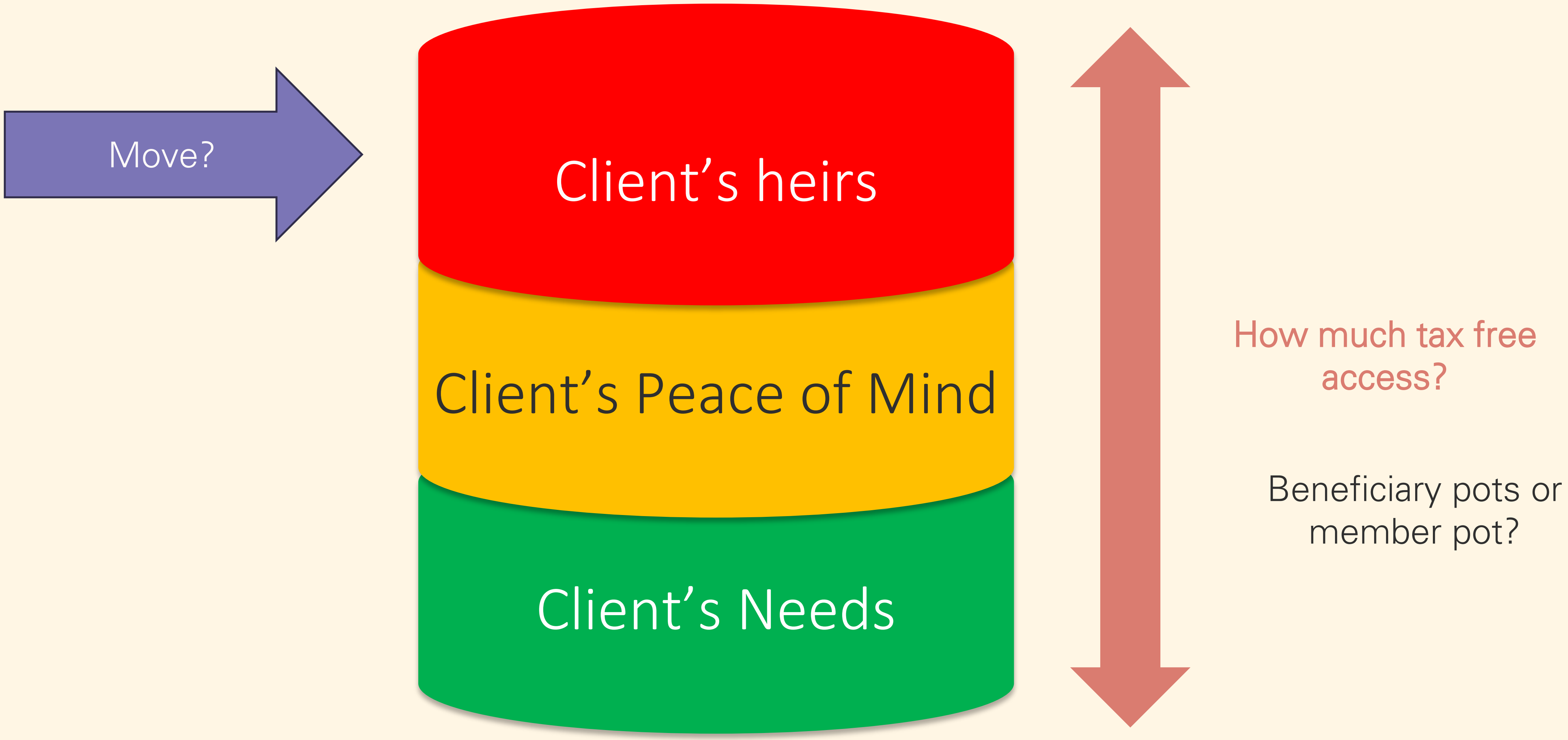
Marginal rate
INCOME TAX

On total value

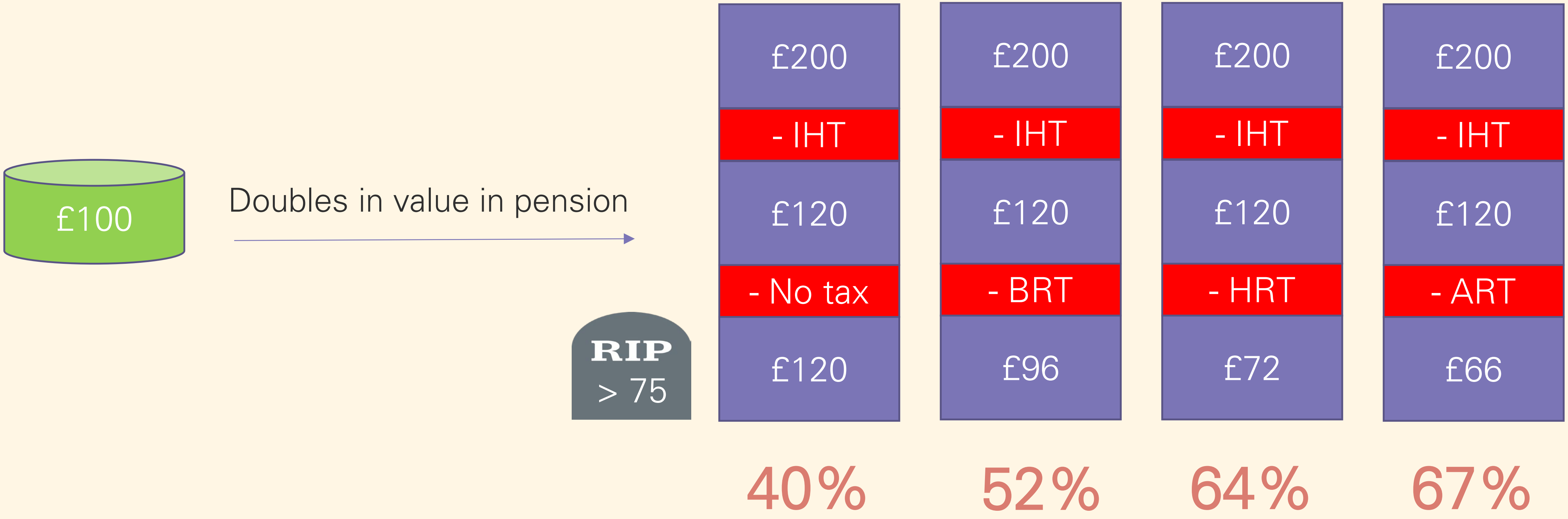
IHT
0% or 6% or 40% world

Income / Gains
0% to 45%
growth & income only

Clients pension pot

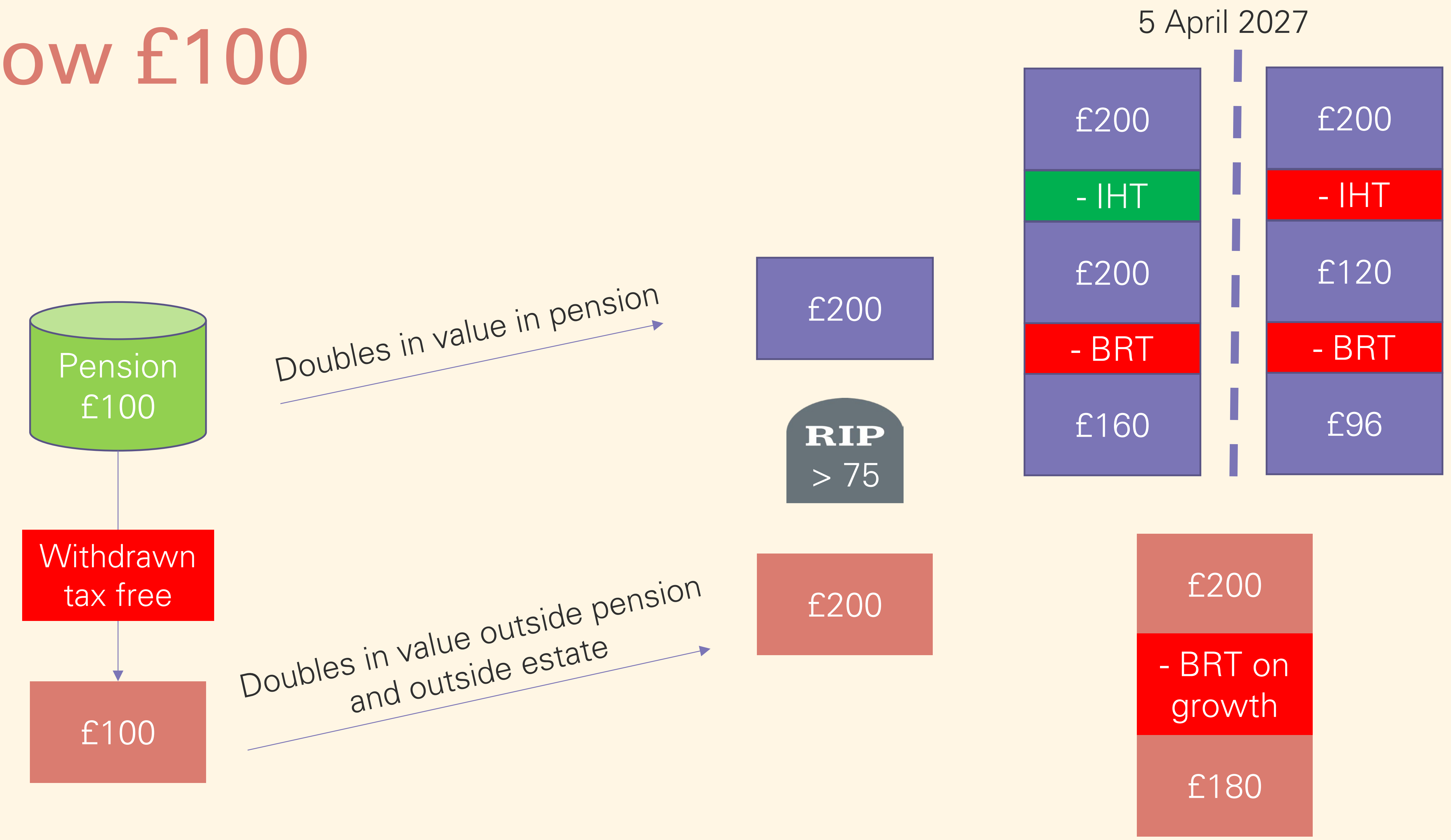


Follow £100



Can you get the pension pot to the next generation with less tax?

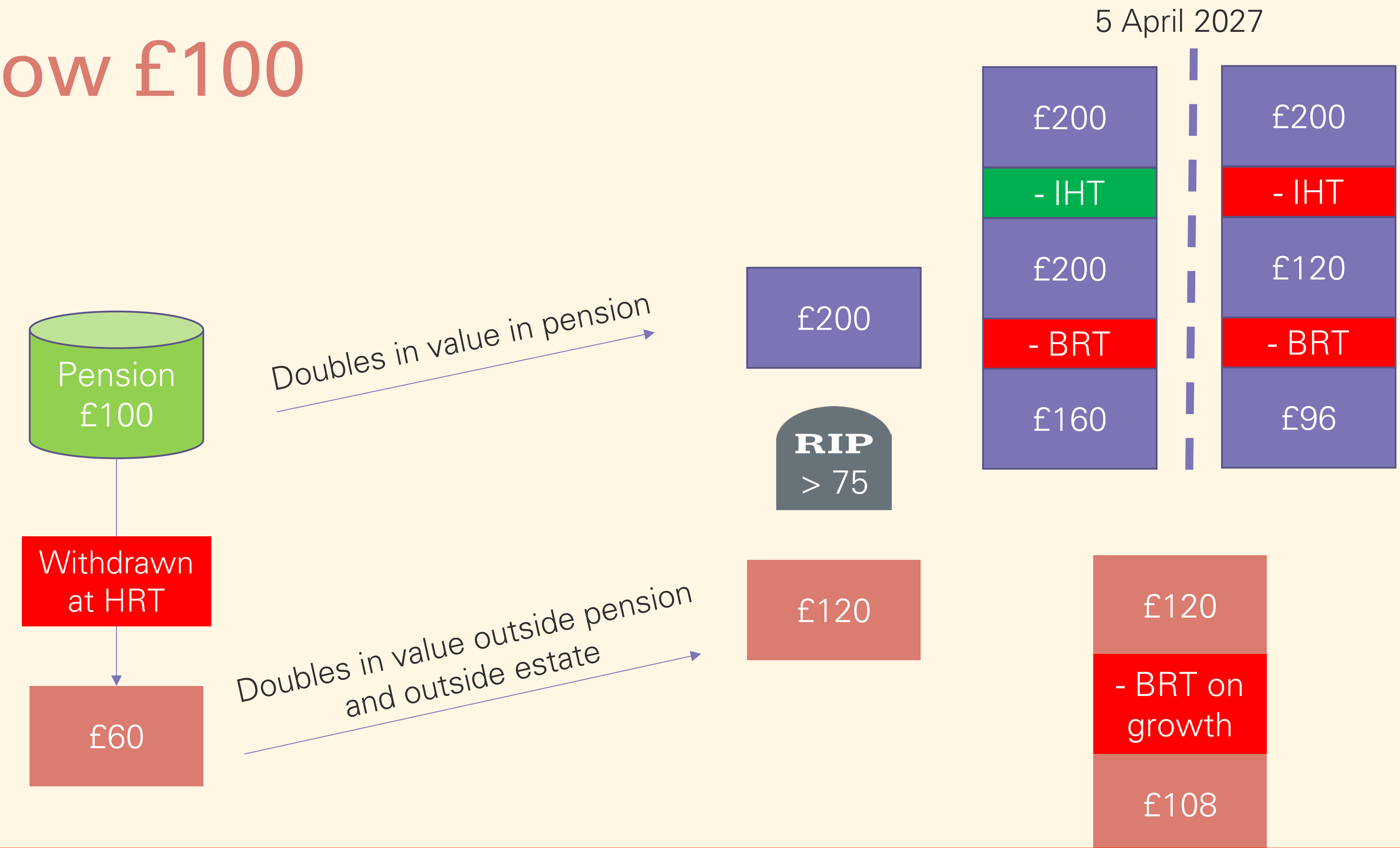
Follow £100



If gift failed it would be 40% IHT on £100 = £40

Scenario		1	2	3	4	5	6	7
		In pension death pre 75	In pension death post 75	Loan trust	Gift	Exempt Gift	Business relief	In pension death post 75 (no IHT)
Growth		5%	5%	5%	5%	5%	3%	5%
Pension value		£100,000	£100,000	£100,000	£100,000	£100,000	£100,000	£100,000
Death before April 2027 (just under 2 years)								
Gross value		£110,250	£110,250	£110,250	£110,250	£110,250	£106,090	£110,250
IHT (assume no NRB)	40%	£0	£0	£40,000	£40,000	£0	£42,436	£0
Income tax	20%	£0	£22,050	£2,050	£2,050	£2,050	£0	£22,050
Net legacy		£110,250	£88,200	£68,200	£68,200	£108,200	£63,654	£88,200
Death after April 2027 (just over 2 years)								
Gross value		£110,250	£110,250	£110,250	£110,250	£110,250	£106,090	£110,250
IHT (assume no NRB)	40%	£44,100	£44,100	£40,000	£40,000	£0	£0	£0
Income tax	20%	£0	£13,230	£2,050	£2,050	£2,050	£0	£22,050
Net legacy		£66,150	£52,920	£68,200	£68,200	£108,200	£106,090	£88,200
Death after April 2032 (just over 7 years)								
Gross value		£140,710	£140,710	£140,710	£140,710	£140,710	£122,987	£140,710
IHT (assume no NRB)	40%	£56,284	£56,284	£40,000	£0	£0	£0	£0
Income tax	20%	£0	£16,885	£8,142	£8,142	£8,142	£0	£28,142
Net legacy		£84,426	£67,541	£92,568	£132,568	£132,568	£122,987	£112,568

Follow £100



If gift failed it would be 40% IHT on £60 = £24

Expressions of Wish

April 27

Pension not included in estate

Leave pension system

- If beneficiary will have "red funds"?
- Exit with no NRB usage
- Bypass Trust or Beneficiary?

Stay in pension system

- no NRB used
- potential for 40% IHT charge on 2nd death?
- spouse excluded?
- beneficiary access limited?
- leave to those who will exhaust?

Pension included in estate

Leave pension system

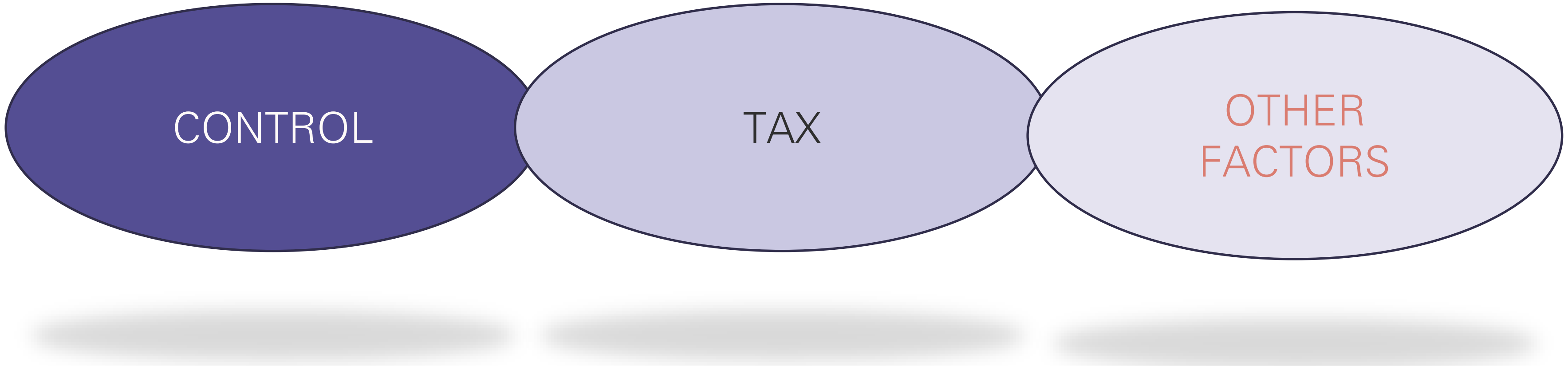
- If beneficiary will have "red funds"?
- Exit may use NRB
- Bypass Trust or Beneficiary?

Stay in pension system

- potential for 40% IHT charge on 2nd death?
- spouse excluded?
- beneficiary access limited?
- leave to those who will exhaust?
- NRB will be used if non-exempt beneficiary

Decide when you want pension to use NRB

Bypass trusts – on the rise?



Will a discretionary bypass trust be a better place than a discretionary pension trust?

Bypass the pension trust?

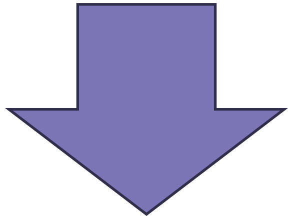
	Bypass Trust	Pension Trust
IHT	up to 6% at 10yrly anniversaries	40% on amount over available NRB on death
Income tax	Only on growth or income received	Income tax on value net of IHT (post 75)
Access	Access for all	Access for beneficiary only. Beneficiary access requires gifting
Control	Your trustees	The pension scheme
Admin	Additional paperwork and reporting	No trust related admin

Nominations?

£500k DC pension

£500k DC pension

Pass to spouse



5 April 2027

Nominations?

5 April 2027

£1m DC pension

Death before 5 April 2027

no IHT due

Death after 5 April 2027

£1m pension in estate for IHT

Nominations (pre 2027 death)

£500k DC pension

Nominate trust on 1st death?

- £500k death benefit avoids 40% IHT where 2nd death occurs after 5 April 2027
- Subject to 6% every 10 years instead
- Spouse has full access if required
- Trust distributions to next generation as opposed to gifts

Re-assess as April 2027 approaches

First in, last out?

£900,000 Estate (2nd death)

Values	ISA	Pension	ISA	Pension	ISA	Pension
Death	£450,000	£450,000	£300,000	£600,000	£600,000	£300,000
Allocated NRB	£325,000	£325,000	£216,667	£433,333	£433,333	£216,667
Subject to IHT	£125,000	£125,000	£83,333	£166,667	£166,667	£83,333
IHT due	£50,000	£50,000	£33,333	£66,667	£66,667	£33,333
Total IHT	£100,000		£100,000		£100,000	
Post IHT Values	£400,000	£400,000	£266,667	£533,333	£533,333	£266,667
Net of IHT value	£800,000		£800,000		£800,000	
Beneficiary Income tax						
20%	£0	£80,000	£0	£106,667	£0	£53,333
Net proceeds	**£720,000**		**£693,333**		**£746,667**	
40%	£0	£160,000	£0	£213,333	£0	£106,667
Net proceeds	**£640,000**		**£586,667**		**£693,333**	
45%	£0	£180,000	£0	£240,000	£0	£120,000
Net proceeds	**£620,000**		**£560,000**		**£680,000**	

The income taken to get to the death values will impact overall results

Wrap it up

To act or not to act

Avoiding post 75 income tax disadvantage	Gifting taxed money	Consolidation
Expression of Wish	Divert funding	Annuity Purchase
Segment clients	Business Relief	

Learning Objectives

By the end of this session, you will be able to:

- Describe the tax treatment of pension schemes on death
- Explain the key elements of creating an IHT plan
- Evaluate potential solutions for individuals whose pensions may be caught up in the IHT net

QUESTION TIME

Thanks for your time

Get in touch with your usual contact if you need further help.

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