



Pension Death Benefits and Lifetime Planning

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When planning for retirement, it is important to make sure that your personal pension scheme provides adequate benefits for your family should you die before receiving your pension - and that proper thought has been given to minimising the inheritance tax (IHT) liability.

Under most personal pension arrangements such benefits fall into a 'master trust' operated by the scheme provider, which will be paid to the person named as the beneficiary.

As such, the funds do not belong to the estate of the deceased and so are outside the scope of IHT.

In the case of married couples, however, the beneficiary is usually the surviving husband or wife. This means that on their subsequent death, any benefits still included in the estate will be subject to IHT.

As an alternative, a 'discretionary trust' could be created during your lifetime into which any death benefits from the pension policy can be paid. The beneficiaries could include your husband or wife, children and grandchildren. In this way, the surviving spouse can benefit from trust income and capital, or even a loan of the trust property.

Because no one person is entitled by right to the trust income or capital, the value of the trust fund is not attributed to any individual for the purpose of calculating IHT when they die.

The discretionary trust can be created with a nominal sum of, say, £10, and other assets can be transferred to the trust at any stage as part of your overall IHT planning strategy.

Because the value of the trust is not attributed to any individual for IHT purposes, HM Revenue and Customs instead apply a periodic charge to IHT on each successive ten year anniversary of the commencement of the trust. However, the trust is eligible for the same IHT exemption as an individual and the charge on the balance over the exemption, if any, is at the rate of just 6%.

This approach can help minimise the 40% tax charge which may otherwise apply, while ensuring that the surviving spouse, or indeed other family members, can benefit from the trust.