

Death benefits and tax

A guide for personal representatives

All occupational pension schemes and personal pension arrangements are subject to tax rules. The rules set limits on the amount of tax-free contributions people can make to a pension scheme, the maximum amount of benefits that can be paid and the way in which those benefits can be taken. This leaflet explains how the rules introduced on 6 April 2006 may affect the benefits payable following the death of a scheme member.

Important Note: This leaflet reflects our understanding of the tax rules at the time of publication and does not set out to give a comprehensive guide to the tax legislation. You should satisfy yourself that this material is still up to date before relying on it. Depending on your personal circumstances you may wish to consider taking independent financial advice.

Lifetime Allowance

Everyone has a “lifetime allowance” (LTA). The LTA is the total value of pension benefits that an individual can take from all pension arrangements (excluding State benefits) without having to pay extra tax. The benefits are valued and assessed at the time the pension is taken. The LTA does not limit the total amount of pension benefits that an individual can be paid in their lifetime.

The Government has set the LTA at a level which means that most people are unlikely to pay this tax. Despite this, everyone’s benefits must be checked against the limit at the time pensions or lump sum benefits are taken. See www.hmrc.gov.uk for details of the LTA, including rates.

Most people will have a standard LTA of 100% but the LTA may be higher if an individual applied to HM Revenue and Customs for an enhanced LTA. Every time a person starts to draw a new pension benefit from a pension scheme, they will use some of their LTA. If there is no LTA left when their benefit becomes payable, they will have to pay extra tax.

Lump sums payable by a pension scheme after the death of a member may also count towards the member’s LTA.

When a pension scheme member dies, the Civil Service pension arrangements may pay either or both of:

- Pensions for dependants
- Lump sum benefits

Pensions for dependants

Pensions payable to dependants following the death of a member do not count towards the LTA of either the deceased member or the person receiving the pension.

Lump sums

The Civil Service pension arrangements may pay a lump sum death benefit when:

- A scheme member dies in service;
- A member with a frozen pension dies before his or her pension comes into payment; or
- A pensioner member dies shortly after his or her pension comes into payment. This is known as a “pension guarantee” payment and represents the balance of pension to be paid during the guarantee period. The guarantee period is 2 years in **classic** and 5 years in **premium**, **classic plus** and **nuvos**.

Lump sum payments made in respect of death in service or before becoming a pensioner will count against the member's LTA.

Pension guarantee payments will normally count against the member's LTA unless he or she had elected for it to be treated as a "pension protection lump sum death benefit". If a pension protection lump sum death benefit is paid, the scheme must deduct tax at 35% before making the payment. But the lump sum will not count against the member's LTA.

However, if the guarantee payment relates to a pension already in payment at 5 April 2006, then no tax is payable. **The member's personal representative is responsible for sorting out the LTA tax position.** Any LTA tax due is payable by the recipients of the lump sums and will be collected from them by HMRC.

What is a personal representative?

The person who is administering the estate of the deceased member.

What must a personal representative do?

- Make contact with any pension schemes that the member belonged to or was receiving pensions from.
- The scheme pension administrator will tell you the date and amount of any lump sum benefit paid in respect of the member's death which will count towards the member's LTA. They will also tell you how much of the LTA was used up by the lump sum. They must give you this information within three months of the payment being made.
- If any pension scheme is paying a lump sum on the death of the scheme member which counts towards the member's LTA, you will need to find out how much lifetime allowance the member had already used up (in total). You can get this information from the member's pension scheme(s) and they should provide this information within 2 months of you asking.

If the member's remaining LTA is insufficient to cover any lump sums paid on their death, you, as the personal representative, must notify HMRC and give them details of the lump sums paid, the schemes that made the payments and the amount on which the LTA tax charge is payable.

Important: Remember that any dependants' pensions payable following the death of the member do not count towards the member's lifetime allowance.

Members aged over 75 on death

- The tax rules do not allow us to pay lump sums in respect of members who are aged 75 or over at the date of death unless the individual was already receiving a pension at 5 April 2006.
- If a pension guarantee payment is due on the member's death, we cannot pay this as a lump sum. We will instead continue to pay the annual pension – for the rest of the guarantee period – to the person(s) nominated to receive the lump sum. We will make these pension payments annually in advance.

You can get further information from the HM Revenue and Customs (HMRC) website: www.hmrc.gov.uk/pensionschemes

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