

## Autumn Budget 2024

### Unused pension funds and Death Benefit Lump Sums to form part of an individual's estate and be brought within the scope of Inheritance Tax effective from 6 April 2027

There had been a lot of rumour and speculation in the press prior to the Budget on 30 October 2024 about what changes the new Government would put in place that would affect pensions. Most of these did not form part of the Budget, but what has been announced in relation to Inheritance Tax is somewhat unexpected.

#### What has been announced?

The Government has announced that from 6 April 2027 most unused pension funds and death benefits will be included within the value of an individual's estate for Inheritance Tax purposes.

#### Government's Rationale

Most estates in the UK do not currently pay Inheritance Tax. It appears therefore that the Government's intention is to make the Inheritance Tax system "fairer" by removing the opportunity for individuals to use pension monies as a vehicle for inheritance tax planning by passing monies on to their beneficiaries untaxed on death. Secondly, the Government states that it wants to ensure that "tax reliefs on pensions are being used for their intended purpose to encourage saving for retirement and later life."

#### What is Inheritance Tax?

Inheritance Tax is a tax on an individual's estate, that is, the property, money and possessions of someone who has died.

There is normally no Inheritance Tax to pay if either:

- the value of an individual's estate is below £325,000
- an individual leaves everything above £325,000 to a spouse, a civil partner, a charity or a community amateur sports club

The standard Inheritance Tax rate is 40% charged on the part of an individual's estate that is above the £325,000 threshold.

There are, however, various other reliefs and exemptions to be taken into account in relation to the calculation of Inheritance Tax.



## What lump sums will likely be affected by this change?

### 1.1. Defined Benefit Schemes

- Lump Sums paid on death whilst in employment (but possibly not those separately insured outside a scheme)
- Lump Sums in respect of Refunds of Contributions paid on death in deferment/or on death in retirement
- Defined Benefit Lump Sum Death Benefits paid on death in retirement (such as a 5 year Guarantee)
- Pension Protections Lump Sum Death Benefit (such as a 5 year Guarantee)
- Uncrystallised Funds Lump Sum Death Benefit (a member's unused Additional Voluntary Contributions "pension pot" when they die)
- Trivial Commutation Lump Sum Death Benefit

### 1.2. Defined Contribution Schemes/arrangements

- Trivial Commutation Lump Sum Death Benefit
- Drawdown fund lump sum death benefit
- Flexi- access drawdown fund lump sum death benefit
- Annuity protection lump sum death benefit

In addition, Dependants annuities, drawdown pensions, short-term flexi-access drawdown annuities, nominee's annuity and successor's annuities will also be included in the value of an individual's estate for Inheritance Tax purposes.

The Defined Contribution pension schemes administered by Cartwright do not permit the payment of most of these types of benefits and members would have to transfer to an alternative arrangement to access annuities and drawdown products.

## What does this mean for pension scheme beneficiaries?

It means that potentially after 6 April 2027, depending on an individual's personal and financial circumstances, some unused pension funds and death benefit lump sums will be liable to Inheritance Tax.

In addition, if the member was over age 75 at the date of death, income tax may also be payable at the recipient's marginal rate if:

- The amount exceeds the Lump Sum and Death Benefit Allowance (of £1,073,100);
- The benefit is paid out more than 2 years after the member's date of death.

Below is a simple, hypothetical example of how Inheritance Tax could apply in respect of a Defined Benefit Lump Sum Death Benefit payable in respect of a Defined Benefit Scheme member on death:



|  | Pre 6/4/2027 position | Post 6/4/2027 position |
|--|-----------------------|------------------------|
| A divorced member dies after 2 years retirement.<br>A Defined Benefit Lump Sum Death Benefit (DBLSDB) is payable (representing 3 years unpaid pension instalments) of:   | £200,000              | £200,000               |
| The Trustees have discretion under the Rules to distribute the lump sum in such proportions and to whom they deem appropriate, but take into account the member's nomination on the Expression of Wishes form. The member nominated that in the event of death, the lump sum should be paid to their only son. |                       |                        |
| Value of the estate  | £400,000              | £400,000               |
| <b>Total value of estate subject to Inheritance Tax</b>  | <b>£400,000</b>       | <b>£600,000</b>        |
| Amount subject to Inheritance Tax above £325,000<br>(Value of estate minus £325,000)   | £ 75,000              | £275,000               |
| <b>40% Inheritance Tax</b>   | <b>£ 30,000</b>       | <b>£110,000</b>        |
| Amount of tax payable by the Scheme Administrator on the DBLSDB of £200,000<br>(£200,000/£600,000 x £110,000 (total tax) =£36,667)   |                       | £ 36,667               |
| Amount of tax payable by the Personal Representative on £400,000<br>£400,000/£600,000 x £110,000 (total tax) =£73,333  |                       | £ 73,333               |
| <b>Net value of estate after Inheritance Tax (i.e. including DBLSDB)</b>   | <b>£570,000</b>       | <b>£490,000</b>        |

## Other changes

As part of these changes, from 6 April 2027 Scheme Administrators of registered pension schemes will become liable for reporting and paying any Inheritance Tax due on unused pension funds and death benefits and liaising with the deceased individuals Personal Representatives in relation to the value of the estate.

## Consultation

The Consultation will run until 22 January 2025.

## What do Trustees need to do?

If Trustees have not already done so, we recommend the following actions are undertaken as soon as possible:

### HMRC's on line services

- They ensure a formal Scheme Administrator is in place for their scheme with an A0 number, who has full access to HMRC's Managing Pension Schemes on-line systems.
- They update all the necessary scheme details on the old pension schemes on-line service (TPSS) system and then enrol and migrate their scheme to HMRC's Managing Pension Schemes system.



- They ensure they associate a Scheme Practitioner to their scheme in order that the Scheme Practitioner may act on their behalf in relation to the reporting and liaising with HMRC, Personal Representatives and scheme beneficiaries, in the future.

### What Cartwright will do?

- Cartwright will assist Trustees with obtaining on-line access and migrating their scheme to Managing Pension Schemes.
- Once the consultation is over and full details of all the changes are known and how they may affect processes and procedures Cartwright will:
  - Advise the Trustees
  - Amend all the reports to the Trustees
  - Amend all the member communications
  - Amend the processes and procedures
  - Amend the IT system
- In making any changes to any processes and procedures, of course, cognisance will be given to all potential Data Protection issues that may occur.

### Cartwright Comment

Having to get more involved with Personal Representatives and the value of a member's estate at death is not a welcome change and could be seen as particularly intrusive at a difficult time. Death cases can be extremely difficult to handle, families and other parties involved are often reluctant to provide information and therefore they have to be handled sensitively, and with care and consideration. It is likely these changes will only delay the settlement of lump sum benefits and complicate further both Trustee and administrators procedures and processes.

These changes also appear to target more wealthy members of pension schemes and those who are unmarried or divorced (i.e. those without a legal spouse or a civil partner) at death.

**If you would like to discuss this matter further, please get in touch with your usual contact at Cartwright.**

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