

## PENSIONS

### USE OF DEFINED CONTRIBUTION SCHEMES IN RETIREMENT AND SUCCESSION PLANNING



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Changes to the pension schemes rules in April 2015 and 2016 offered a new option for individuals to consider as part of their retirement and succession planning strategy. In this article we summarise the recent changes and the main points to bear in mind in respect of defined contribution schemes.

#### RELAXATION OF TAX CHARGES FOR PENSION FUNDS ON DEATH AFTER AGE 75

It has long been the case that if an individual dies before taking any pension benefits (and before age 75), the fund remains outside the individual's estate for inheritance tax (IHT) purposes and there is no exit charge on funds paid to their nominated beneficiaries. However, under the old rules, for those who died after reaching age 75 or after they had begun to take benefits, there was a flat 55% exit charge on lump sums paid out to beneficiaries.

From 6 April 2015, the 55% charge for lump sum payments was reduced to 45%, and then entirely abolished from 6 April 2016. There is now therefore no charge on death, whether funds are paid out as lump sums or left to beneficiaries as a flexi-access fund. However, beneficiaries who take income from the inherited pot will pay tax on it at their marginal rates of income tax.

There is an overriding rule that the fund must be dealt with within two years of notification of the member's death.



#### PLANNING CONSIDERATIONS

Members of a DC scheme can now nominate someone to inherit the unpaid pension fund as a "nominee's flexi-access drawdown account". This nominee can be any person (not necessarily a dependant), with no age restrictions. Therefore, children could also be nominated. Such nominees will now have access to income at any age.

The beneficiary can also nominate a successor so that any funds remaining in the drawdown fund at their death can be passed on to their children or chosen individuals. Again, if the beneficiary dies before age 75, the successors inheriting the drawdown fund can access it tax-free but, if they inherit later, the funds are taxed as income when withdrawn.

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The potential advantages of being able to pass on pension funds include:

- Inherited funds that remain invested will continue to benefit from tax-free growth until the beneficiary withdraws them. The pot can even be returned to beneficiaries (which does not impinge on their ability to fund a pension) or left for future generations.
- This effective 'IHT exemption' of up to £1.055 million for individuals and £2.11 million for couples should be considered by anyone who will be able to fund their retirement by other means. Tax savings will depend on the income levels of beneficiaries.

If an individual has no dependants, it is possible to nominate a charity to receive any remaining pension funds tax-free on death.

Many individuals may need to revisit their current plan. This can include updating their Wills and letters of wishes to their pension fund trustees to ensure that their intended beneficiaries get the full benefit of any pension funds remaining at their death.

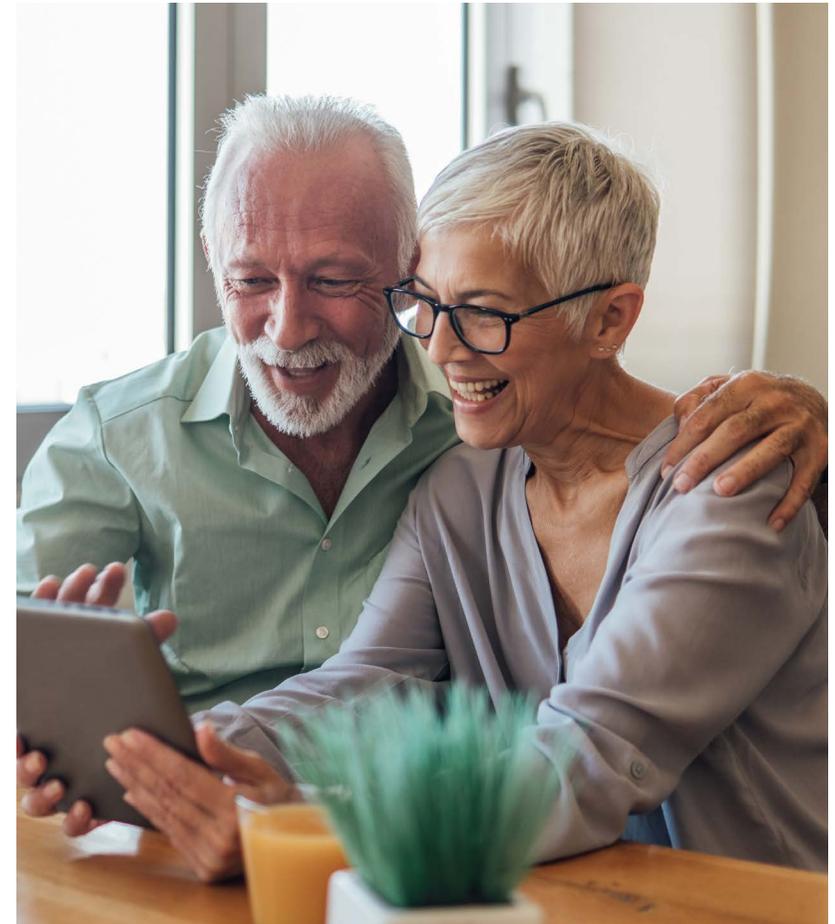
Personal trusts are also used to hold pension interests.

What is appropriate to each case will be based on the individual's personal circumstances.

### DEFINED BENEFIT SCHEMES

Members of defined benefit (final salary) schemes may be able to transfer entitlements to a personal pension to benefit from the relaxed rules. However, it is a legal requirement that individuals must take professional advice from a qualified independent financial adviser before any transfers out of final salary schemes can be made.

When planning for the future, all factors (including transfer costs and the loss of a guaranteed income) will need to be carefully considered, and professional investment advice should be taken as appropriate. It is also vital for individuals to take tax advice to plan for a tax-efficient retirement and to ensure that they can pass on funds to their family if they choose, without penal tax charges. Such transfers may only be appropriate in particular circumstances, such as where there is a short life expectancy.



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