

## Fact Sheet 5

### Benefits payable on your death under Your SIPP

The benefits that can be provided on your death will depend on whether, at the time you die, you:

- were under age 75 and had not started taking benefits from your SIPP (see below),
- were under age 75 and had started taking benefits direct from your SIPP through income withdrawals (see below),
- had taken your SIPP benefits by buying a Lifetime Annuity (see page 2), or
- were over age 75 and still had vested funds in your SIPP providing income withdrawal as ASP (see pages 3 and 4).

There are also stricter rules governing any Protected Rights you hold in your SIPP (our Fact sheet 3 explains more about Protected Rights).

#### Expression of Wish

If you die before age 75 we decide who will receive a benefit from your SIPP on your death, and in what form those benefits will take (within the tax rules). However, when you set up a SIPP we ask you to complete an Expression of Wish form indicating who you wish to benefit from any remaining SIPP funds on your death. We will follow your Expression of Wish, unless there are reasonable grounds not to. Where you have nominated a spouse / dependant as your beneficiary but have not indicated the form you wish benefits to be paid (lump sum / pension) we will generally give the beneficiary a choice, where there is one.

You can change this Expression of Wish at any time.

You can nominate more than one beneficiary if you wish – this does not have to be your spouse / dependants.

If you die after age 75 in ASP, the position is different. A new Expression of Wish will be required at age 75.

#### What happens if I die before age 75 and have not started taking benefits from my SIPP?

If you hold any Protected Rights in your SIPP then, if you are survived by a spouse or civil partner, these funds must currently be used to provide them with a pension benefit. If you are not survived by such a person then the options available are detailed below.

Any funds that are not Protected Rights remaining in your unvested SIPP Segments (see our Fact Sheet 3) can be used to provide:

- any beneficiary (including, but not limited to, your dependants) with a lump sum benefit; this will be paid taxfree, provided within your remaining available Lifetime Allowance (see page 3), or
- your surviving dependant(s) with a pension benefit, either direct from the SIPP through income withdrawal or by purchasing an annuity from an insurance company ('dependant' is defined overleaf).

Any pension will be taxable income of your dependant, with the tax due deducted and accounted through PAYE. A pension benefit cannot be provided to someone who is not your dependant.

#### What happens if I die before age 75 whilst in income withdrawal?

Any funds remaining in your vested Segments can be distributed in the same way as detailed above for unvested Segments (including any restrictions on Protected Rights) but any lump sum paid will be taxed at a rate of 35%. We must deduct the due tax before payment and account for it direct to HMRC. This taxed lump sum will not count for Lifetime Allowance purposes.

If you have vested some but not all of your Segments under your SIPP, then any lump sum paid from those unvested Segments will still be tax-free (provided within your available Lifetime Allowance).

### Example 1

John dies in March 2008, aged 58. He is survived by a wife, and two grown-up sons.

He has vested 400 of his SIPP Segments through income withdrawal; these vested Segments hold £200,000 on his death. His remaining 600 unvested Segments hold funds worth £350,000. None of these funds are Protected Rights.

John has nominated that 50% of his remaining funds be used to provide for his wife, with the remaining 50% split equally between his sons. His wife is his dependant, but his sons are not dependent on him.

His wife has the option of taking a pension benefit, but decides on taking the lump sum. His sons must take a lump sum. It has been agreed that the vested and unvested funds will be split between the three proportionately (although this does not have to be the case).

The £200,000 lump sum paid from the vested funds is subject to a 35% tax charge. The £350,000 unvested funds are paid tax-free, but if John had less than £350,000 of Lifetime Allowance left on death, the three would be liable outside the SIPP to a 55% tax charge on the amount paid not covered by John's remaining Lifetime Allowance (split proportionately - see page 3).

The £70,000 tax due on the £200,000 (35%) vested funds is deducted, leaving a net lump sum payable of £480,000 ( $\{£200,000 - £70,000\} + £350,000$ ). Julie is paid £240,000 and the two sons £120,000 each.

### What happens if I die after I have purchased a Lifetime Annuity?

If you die after buying a Lifetime Annuity, then no pension or lump sum will be paid from the SIPP in relation to the Segments used to buy that annuity.

Income payments will only continue under the terms of that annuity contract if you:

- are survived by a dependant and you bought a joint-life annuity, or
- purchased an annuity with a guarantee and you died within the guarantee period – payments would continue to the end of that guaranteed period to the nominated beneficiary (subject to income tax).

If an annuity with 'value protection' was purchased a lump sum may be payable on your death if you died before age 75 (taxed at 35%) under the terms of that contract. No lump sum can be paid if you die after age 75. The tax due will be deducted and accounted for by the insurance company before payment.

### Who will be my dependant?

A 'dependant' is defined in the tax legislation.

Your children (including an adopted child) will be your dependant if under age 23, or older where dependent on you due to physical or mental impairment.

An adult (age 23 or over) who is not your child is your dependant if

- they are your spouse or civil partner,
- they are financially or physically dependent on you, or
- we are satisfied their financial relationship with you is one of mutual dependence.

## How would any dependant pension be paid?

If the dependant's pension is being provided direct from the SIPP through income withdrawal then:

- we will calculate a new maximum income payable based on your dependant's own circumstances (i.e. their sex and age) – the maximum is calculated and reviewed differently depending on whether they are under or over age 75 (similarly as detailed in Fact sheet 4), and
- if they are over age 75 and go into ASP, they will be bound by the same ASP minimum payment requirements (see Fact sheet 4).

If the dependant's pension is secured by purchasing an annuity contract with an insurance company, that contract cannot provide for a lump sum or pension benefit to continue on their death, or be guaranteed on that dependant's life. No benefit will be payable from the SIPP on their death.

If your dependant takes income withdrawals they may buy an annuity at any time with those vested SIPP funds allocated to them.

If a person is dependant on you purely because they are under age 23, then a pension must stop once they reach age 23. If being paid as income withdrawal from the SIPP the maximum payable will reflect the fact payments must stop at age 23, and we may be able to pay any remaining funds at that time as a lump sum taxed at 35% (the position would be the same as detailed on page 4 where a dependant dies). For any other dependant, an annuity must be paid for life (although a spouse's annuity can provide for income to stop on re-marriage).

## Do I or my beneficiaries have to worry about the Lifetime Allowance on my death?

The Lifetime Allowance (see Fact sheet 3) will only be an issue on your death where you die before age 75 and a lump sum is paid from unvested Segments held in your SIPP.

Here, as the lump sum is paid nominally tax-free, the payment counts against your Lifetime Allowance. If the lump sum exceeds your remaining available Lifetime Allowance when you died then the person we pay the lump sum to will be subject to a tax charge of 55% on the excess. Your personal representative is responsible for checking whether there is a Lifetime Allowance charge due on your death (not us).

Any pension benefit provided to your dependants does not count either against your or your dependant's Lifetime Allowance. Any lump sum paid from vested funds (taxed at 35%) also does not count.

## What happens to any funds remaining if I die after age 75 in ASP?

If you are survived by a dependant then the remaining funds must be used to provide them with a pension benefit, either by buying an annuity from an insurance company, which will provide them with an income direct, or instead the dependant can opt to take the income direct from the SIPP through income withdrawal.

If you are not survived by a dependant then the only option is for the remaining funds to be paid to a registered charity or charities. We will ask you to nominate a charity or charities before going into ASP. This may also be an option if you are survived by a dependant when they die, if they too go into ASP. If the monies are not used for charitable purposes by the charity there will be tax charges.

Please note that a 'dependant' is narrowly defined in the tax legislation (see page 2). It will not generally cover, for example, a son or daughter over age 23. We would also re-iterate that any pension provided to a child of yours under the age of 23 must stop once they reach age 23, unless they were also dependent on you because of physical or mental impairment. The position then would be the same as detailed on the next page when a dependant dies in income withdrawal.

If remaining funds are not used in the above ways there are severe tax consequences on both the beneficiary personally and your SIPP, including potentially inheritance tax (IHT) being due. These tax charges in aggregate could be as high as 82% of the fund remaining.

IHT may also be applied to your SIPP if the funds are not distributed or allocated in the above way within 6 months of the end of the month in which you die in ASP or where you are survived by a dependant who is only dependant on you (through mutual dependency (not a spouse/civil partner or a full financial dependant)). Your SIPP funds would be viewed as the 'top-slice' of your estate (so potentially all subject to a 40% tax), and any IHT due would be met by the SIPP. If there was any unused IHT nilrate band available outside your SIPP then credit will be given to the ASP funds being charged to IHT. Any unused nil-rate band can be indexed up in certain circumstances (possibly quite generously). HMRC calculate the IHT due and charge us direct based on the returns we and your personal representative make.

***We cannot provide you with advice on your (and your SIPP's) possible IHT position on death.***

If any remaining funds on death are to fall outside IHT the investments held in your SIPP after age 75 need to be sufficiently liquid to allow quick distribution. If you hold property, for example, it is unlikely this would be sold in time to make payment to charity, where required. We can make no guarantees that we can meet the deadline, and the risk that IHT may be applied to your SIPP funds on your death in ASP is a risk you must accept and sign-up to before going into ASP.

### **If on my death my dependant decides to take a pension through income withdrawal, what happens to any remaining funds in my SIPP when they die?**

If they die **before age 75**, then

- the remaining vested funds would be paid as a lump sum to the nominated beneficiary, subject to a 35% tax charge (deducted and accounted for by us).
- if you had more than one surviving dependant on your death, an alternative option would be for them to be provided with a pension benefit (if still alive); the position on their subsequent death would be the same as on the death of the first dependant, but depending on their age.
- if you had previously died after the age of 75 in ASP, the remaining funds at death may be subject to Inheritance Tax (IHT) as well (see the next page). Here, any IHT due would be deducted from your SIPP funds first, with the remaining funds being paid out to the beneficiary net of the 35% tax due.

If they die **after age 75** in ASP, then

- the remaining funds must be paid to a registered charity, unless you have other surviving dependants.
- if there was another surviving dependant of yours they must be provided with a pension benefit with those funds; the position on their subsequent death would be the same as on the death of the first dependant, but depending on their age.
- if the remaining funds are not paid to charity within 6 months of the end of the month your dependant dies in then IHT may be due.

If you had previously died

- before age 75, then we would write to your dependant near age 75 outlining their options, and asking them to nominate a charity - if any IHT became due on their death in ASP, this would be based on your beneficiary's circumstances on their death (i.e. the value of their estate outside the SIPP).
- after age 75 in ASP, then you will have made the charity nomination when you first went into ASP and your dependant may only vary your nomination if you agreed to this - if any IHT became due, this would be based on your circumstances on death (not your beneficiary's).

### If I am survived by a dependant is IHT an issue in the future if there are still funds held in my SIPP when they die (and if so how would any IHT liability be calculated)?

IHT will only be charged on the remaining SIPP funds held upon the death of your dependant where

- they are under age 75 when they die and you previously died after age 75 in ASP, or
- either you or your dependant died after age 75 and the remaining funds are not paid to charity within 6 months from the end of the month your dependant died in.

Where you had previously died after age 75 in ASP then any chargeable funds remaining on the death of your dependant (no matter their age) are still viewed as the 'top-slice' of your estate, not your dependant's. If the value of *your* chargeable estate on your earlier death was less than the current IHT threshold at the time of your dependant's death (£300,000 as at 2007/08) that unused nil-rate band is credited to the chargeable funds at the time your dependant died. This unused nil-rate band may again be indexed up in some cases.

Where you had previously died before age 75 then any chargeable ASP funds remaining on the death of your dependant after age 75 in ASP is treated as the 'top-slice' of *your dependant's* estate. Again, if their nil-rate band is not used up outside the SIPP credit is passed on to the SIPP.

Any funds not covered by any nil-rate band passed on to the SIPP would be charged to IHT, paid by the SIPP.

#### Example 1

Julie goes into ASP on her 75th birthday. She draws her annual maximum of £12,000.

Julie dies on her 77th birthday in May 2007. She is survived by a husband, John, aged 72. Her children are not dependants, as over age 23. John must continue taking a pension from the SIPP; he opts to take income withdrawals. A fresh maximum is calculated based on his circumstances (as male and under 75, his maximum increases to £15,000). He must opt by 30th November 2007 if IHT is not to be an issue.

If John died before reaching age 75 (leaving, say, £100,000 in the SIPP) the remaining funds would be paid as a lump sum following Julie's expression of wish. IHT may be due first, which we would deduct and account for. The remaining £100,000 is treated as the top-slice of Julie's estate (not John's) – Julie had used up her nil-rate band on her death, so 40% is due on the whole £100,000 (if her estate was under the IHT threshold, credit for the unused nil-rate band would be given). The remaining £60,000 is subject to a 35% tax charge (£21,000) - we deduct this and pay the nominated beneficiary £39,000 net.

If John had reached age 75 and decided to go into ASP, then we would calculate a fresh annual maximum on his 75th birthday. He would be required to draw a minimum income, with tax due on his SIPP if not paid. This maximum and minimum would be reviewed every birthday. If he died still in ASP, as there would be no more surviving dependants of Julie, the remaining monies would be paid to charity (as nominated by Julie). This would be tax-free, provided paid within 6 months of the end of the month which John dies in (if later, IHT would be due as Julie had previously used up her IHT nil-rate band).

### Do I have to worry about IHT being due if I die before age 75?

Our understanding is that no IHT will arise on any lump sum death benefit paid from any funds held in your SIPP that are **not** Protected Rights where you die before age 75, providing that you were in normal health at the time you chose to take income withdrawals (where relevant) and that you did not change the value of your withdrawals later because your health deteriorated.

If you have no surviving spouse / civil partner then your Protected Rights can be paid as a lump sum on your death, where you die before age 75. This must under DWP law be paid to the person you nominated in your Expression of Wish, or to your estate where you have not so nominated. We do not have discretion with Protected Rights, as with your other SIPP funds. This means the lump sum paid from any Protected Rights is likely to count against your estate for IHT purposes. We cannot advise you on your IHT position.

If you (or your dependant) continue into ASP after age 75, there are IHT issues, as discussed above.

**PLEASE NOTE:** This fact sheet is based on Pointon York SIPP Solutions Limited's understanding of current legislation and HMRC Guidance at the time of print. It should not be relied upon as a statement of law, or for advice purposes. Whilst every effort has been made to ensure that the information is correct, we cannot accept responsibility or liability for any omission or inaccuracy provided in this document. Pointon York SIPP Solutions Limited is authorised and regulated by the FSA.