

Making death benefits and the lifetime allowance easier

May 2016

Introduction

Providing death benefits through a registered pension scheme may have adverse tax consequences for high-earners. Certain lump sums paid on death are tested against the deceased member's lifetime allowance. A tax charge is payable if the allowance is exceeded. In addition, those individuals who have preserved a higher than standard lifetime allowance through enhanced or fixed protection may lose that valuable protection if death benefits are provided for them through a registered pension scheme.

The lifetime allowance reached its peak of £1.8m in 2010, but is set to fall from £1.25m to £1m on 6 April 2016. More and more individuals are affected. This means that employers should review the way that death in service lump sum cover is provided, in particular for high-earners.

Triggering of the lifetime allowance charge

Certain events under a registered pension scheme trigger a test against a member's lifetime allowance. Those events include the payment of a lump sum on the death of a member under age 75 if, broadly, he or she has not yet taken any benefits from the relevant pension arrangement. Any employee whose death in service lump sum might take him or her over the lifetime allowance is affected - particularly high-earners with death benefits based on a high multiple of salary. The employee may already have used up some of his lifetime allowance before death, eg by drawing income from a separate defined contribution pot.

Loss of enhanced and fixed protection

Enhanced protection and fixed protection allow certain high-earners to continue to benefit from the higher levels of lifetime allowance that were available in the past. An increasing number will be affected with the fall in the lifetime allowance to £1m. However, the provision of a death benefit from a registered pension scheme will usually lead to that protection being lost. There is an exception where the death benefit takes the form of a defined benefit promise that was made before the protection took effect (eg the employee still has life cover under a closed DB scheme). Changes to death benefits, or the provision of a death benefit for a new employee, will generally lead to any protection being lost.

Moving employees to an excepted group life scheme

One solution to the tax points identified above is an excepted group life scheme. That is an arrangement for providing the whole workforce or a group of employees with lump sums on death in service. The advantage of this sort of scheme is that it falls outside the lifetime allowance regime, which applies only to registered pension schemes. In addition, excepted group life schemes are not subject to the registration and reporting requirements that apply to registered pension schemes.

It is relatively easy to set up this sort of scheme, although certain points need to be handled carefully to ensure there are no unintended tax consequences. Please contact your usual Pinsent Masons adviser if you wish to know more.

Continued on next page >

Making death benefits and the lifetime allowance easier

May 2016

Pensions law can be tricky... but it doesn't have to be. These 'making it easier' guides explain key issues in simple terms, giving practical help to trustees and employers.

The series is growing; additional copies can be downloaded from www.pinsentmasons.com

Current topics include: Using advisers; Scheme changes and Becoming a trustee

Comments and ideas for further topics are welcome...

Email: [Stephen Scholefield](mailto:Stephen.Scholefield@pinsentmasons.com)



This note does not constitute legal advice. Specific legal advice should be taken before acting on any of the topics covered.

Pinsent Masons LLP is a limited liability partnership registered in England & Wales (registered number: OC333653) authorised and regulated by the Solicitors Regulation Authority and the appropriate regulatory body in the other jurisdictions in which it operates. The word 'partner', used in relation to the LLP, refers to a member of the LLP or an employee or consultant of the LLP or any affiliated firm of equivalent standing. A list of the members of the LLP, and of those non-members who are designated as partners, is displayed at the LLP's registered office: 30 Crown Place, London EC2A 4ES, United Kingdom. We use 'Pinsent Masons' to refer to Pinsent Masons LLP, its subsidiaries and any affiliates which it or its partners operate as separate businesses for regulatory or other reasons. Reference to 'Pinsent Masons' is to Pinsent Masons LLP and/or one or more of those subsidiaries or affiliates as the context requires.

© Pinsent Masons LLP 2016.

For a full list of our locations around the globe please visit our websites: www.pinsentmasons.com and www.Out-Law.com.