VIEWPOINT

IHT Consultation: A simpler future for pensions

MUFG Retirement Solutions recently responded to His Majesty's Government's consultation on proposals to improve the consistency of treatment of pension benefits payable upon death.

MUFG Retirement Solutions manages pension benefits for over 2.1 million individuals across master trusts and defined benefit arrangements in the UK, and more than 12.5 million members globally.

In our response, we proposed a simpler, more efficient means approach to achieving the Government's objectives: ensuring fairness, reducing public financial liability, and streamlining processes for all stakeholders.

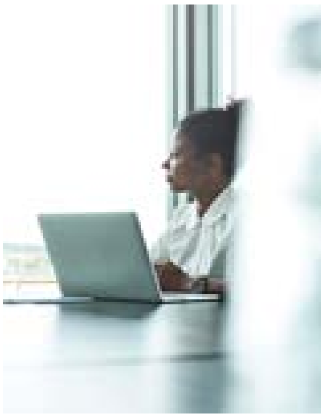
We believe our recommendations simplify the current proposals while aligning with the policy's original intentions. The three key changes we suggest include:

1. **Extending death registration** to include the person managing the deceased's financial affairs
2. **Making all lump sum death benefits** payable to the estate and subject to Inheritance Tax (IHT)
3. **Restricting inheritance of funds** in drawdown to legally recognised partners

1. Registration of Death Changes

To implement the Government's proposals effectively, it is essential to identify the individual managing the deceased's financial affairs. Not all estates go through probate, and in some cases lack immediate family members to handle these matters.

Recording a designated contact person responsible for financial affairs, would streamline settlement processes within the pensions industry, creating a single point of contact for HMRC, life assurance providers, and creditors. This simple but impactful change would make other reforms easier to implement and significantly improve overall efficiency.



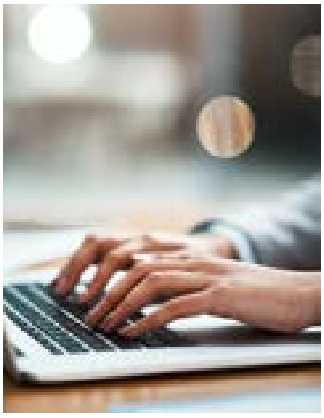
2. Subjecting Lump Sum Pension Death Benefits to IHT

The Government's proposal subjects pension benefits that have not been previously taxed, to inheritance tax when paid as a lump sum. However, we believe benefits designated to continue as income, such as scheme pensions or annuities, should not be treated as a lump sum for IHT purposes, as this would create tax liabilities without providing the liquidity needed to settle them. These income payments would remain subject to income tax when received by the beneficiary.

Funds in drawdown, which can be paid as either a lump sum or income, should be taxed accordingly. If paid as a lump sum, they should be included in the estate for IHT; if paid as income, they should be taxed as income. Restricting income drawdown to legally recognised partners, such as spouses or civil partners, upholds the principle that asset transfers between legal partners are exempt from inheritance tax.

Currently, there are different tax treatments for lump sum death benefits depending on the type of pension arrangement. For example, benefits paid under discretionary trusts are excluded from the estate, while statutory or contractual pension schemes are not. We recommend removing the distinction between lump sums paid before and after age 75 for IHT purposes to simplify the process and prevent double taxation.

Additionally, we propose that pension lump sum death benefits be paid directly to the estate or nominated charity rather than under discretionary trusts. This approach would create consistency across pension provisions, avoid complex changes to trust law, and ensure these benefits are subject to IHT. It would also help cover funeral and testamentary expenses, reduce reliance on the Social Fund and ensure creditors are paid from the estate.



3. Restricting the Use of Drawdown for Inheritance Purposes

Currently, nominees' drawdown allows pension funds to be passed down across generations, often outside the scope of inheritance tax. While this arrangement benefits some individuals, it also creates a loophole that enables pension wealth to be transferred without being subject to appropriate taxation.

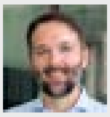
We propose restricting nominees' drawdown to specific cases, such as provision for minors or adult individuals who are unable to support themselves. These exceptional circumstances should be managed within the pension scheme to ensure appropriate allocation of funds. In all other situations, pension benefits should either be included in the deceased's estate or be paid to a legally recognised partner.

Removing the use of nominees' drawdown for inheritance purposes would close this loophole. It would align with the Government's policy of exempting transfers between legal partners from inheritance tax while ensuring that other wealth transfers are taxed fairly. This restriction would prevent pension funds from serving as a tax shelter while still allowing flexibility for innovative solutions in limited, necessary cases.

In conclusion, these three straightforward changes would support the Government's objectives of subjecting untaxed lump sum death benefits to inheritance tax while simplifying the process. This approach eliminates the need for complex changes to trust law and removes the risk of double taxation, particularly in cases where pension income is already subject to PAYE at the point of payment. It would also bring pension benefits into the estate in a transparent and manageable way, without the need for multiple parties to assess and settle tax liabilities.

This solution reduces costs for pension providers, simplifies administration, and ensures fairness in the treatment of pension benefits upon death. Additionally, it also provides benefits such as reducing reliance on the Social Fund and ensuring creditors can be paid. In short, we believe this is a simpler, more cost-effective way to achieve the desired policy outcomes.

We addressed the consultation questions with these proposals in mind and look forward to further discussion on how these changes can be implemented.



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