ABI Technical Q&A on Pensions and IHT Points: Consolidated version

In 2010, the ABI Investment Products Tax Working Group began the process of clarifying key issues relating to pensions and inheritance tax with HMRC. This has been a continuing process with the first guidance published on 11 May 2010. This paper consolidates that guidance with some recently answered questions.

The Q&As from number 3 onwards do not deal with post-1988 pensions which are created by deed poll/board resolution. In the scenarios from number 3 onwards, the contract-based pensions are retirement annuity contracts.

1 Meaning of "estate" and treatment of LSDB paid as a result of discretion

Where pension scheme administrators have discretion over payment of the LSDB from a trust-based pension, IHTM17123 sets out the position involving a 2 year period for the scheme administrators to consider how to exercise their discretion. It is possible that the scheme administrators choose to exercise their discretion and pay the LSDB to the deceased's executors (in the knowledge that this will be distributed either according to the rules of intestacy or to certain beneficiaries under the deceased's Will). Since payment of the LSDB results from the exercise of the scheme administrator's discretion, we consider that the LSDB does not form part of the deceased's estate on death in terms of s 5 IHTA 1984 and as such no IHT arises either on the transfer from the scheme administrators to the deceased's executors (if within 2 years of date of death) nor on the onward distribution of the LSDB by the deceased's executors.

Question 1a: Can HMRC confirm that they agree with this interpretation?

Answer: Confirmed.

Question 1b: Can HMRC confirm that the IHT position is the same, where the LSDB is paid from a contract-based pension scheme and the scheme administrators similarly make a payment of the LSDB to the deceased's executors in exercise of their discretion?

Answer: Confirmed.

2 Number of settlements, nil rate bands and ten year anniversaries

IHTM17126 deals with the reference date for ten year anniversaries in two different scenarios. One scenario involves a trust-based pension scheme with discretionary powers which makes a discretionary payment to a recipient settlement. IHTM17126 states that ten year charges for the recipient settlement will be taken with reference to the date the member first joined the original pension scheme.

Example : X has three employments during his lifetime, each with individual pension schemes (these are all trust-based pension schemes with discretionary powers). For ease of reference, assume X joined each scheme on 1 January 1980, 1 June 1990 and 1 December 2000. To keep his arrangements as tidy as possible for his family in the event of his death, X sets up one family trust (ie. recipient settlement) with £100 on 1 September 2009. He signs a non-binding letter of wishes for each of his three pension schemes to indicate his preference that the LSDB should be paid to his family trust in the event of his death. X then dies on 10 January 2010 and the pension scheme administrators for all three schemes exercise their powers to pay the LSDB to the X Family Trust within 2 years of death.

Question 2a: Applying the analysis in IHTM17126, there are 4 potential reference dates for ten year anniversaries here: 1 January 2020, 1 June 2010, 1 September 2019 (in relation to the initial £100 gift) and 1 December 2010. Can HMRC confirm its analysis of the scenario here in relation to the number of ten year anniversary dates here?

Answer: Confirmed s81 IHTA applies to give 4 ten year anniversary (tya) dates.

Question 2b: As a follow-on point, what is HMRC's analysis in relation to the available nil rate bands in this scenario? Whilst there is one recipient trust, there are three "feeder" pension scheme settlements, which prompts a query over whether the analysis here is of four settlements, each of which has its own nil rate band as the deceased joined each scheme more than seven years after his last pension scheme joining date, and created the X family trust more than seven years after taking up his last employment.

Answer: Confirmed 4 settlements each with its own nil rate band.

3 Contract-based pension scheme

Taking the facts in 2a above, but with three "feeder" contract-based pension schemes rather than trust-based pension schemes, does HMRC agree with the analysis that there is only one settlement with one nil rate band for IHT purposes (subject to the settlor's cumulative total when he created that settlement), with a commencement date which relates to the recipient settlement only?

Answer: Confirmed. S81IHTA cannot apply in this scenario as there is no initial settlement for IHT purposes and so no movement of property from one settlement to another.

4 SIPP consolidation scenario with trust-based "feeder" pensions

A trust-based pension 1 1988		
B trust-based pension 2 1996	D consolidated into trust-based SIPP in February 2008	E discretionary trust set up with £100 in March 2008
C trust-based pension 3 2004		

The scenario here is that X starts with 3 different pension policies, all of which are trust-based in this example. In February 2008, he consolidates them into a SIPP. In March 2008, he creates a discretionary trust with £100 and a letter of wishes (non-binding) is given to the trustees of the SIPP indicating X's preference that any LSDB should be paid to the discretionary trust. X then dies in March 2010 and the LSDB is paid to the discretionary trust. The question arises as to the number of settlements and nil rate bands in this scenario.

Assume two additional points:

4i there are no new pension contributions paid into pension D – the SIPP is a pure consolidation exercise;

4ii alternatively, there are new pension contributions paid into pension D.

Question 4a: Does HMRC agree with the analysis that in 4i, there are 4 settlements, namely the trusts in A, B, C and E? In this analysis, the SIPP at D is ignored since there were no new pension contributions at that stage. The funds ultimately held in trust E therefore represent 4 settlements, each with a different ten year anniversary date. Settlements A, B and C have a ten year anniversary date with reference to the date the deceased took out the original pensions of A, B and C. The settlement at E has a TYA relating to the date the discretionary trust was created with the £100 cash gift. Can HMRC confirm if it agrees with this analysis?

Answer: Confirmed.

Question 4b: Does HMRC agree with the analysis that in 4ii, there are 5 settlements, namely the trusts in A, B, C, D and E? The contrast with the scenario in question 4a is that in 4b the SIPP does count as a settlement since new pension contributions were made. Can HMRC confirm if it agrees with this analysis?

Answer: Confirmed.

Question 4c: Where there are multiple settlements, as found in both questions 4a and 4b, the administrative task facing the trustees of E could involve multiple IHT100 forms at ten year anniversaries. Does HMRC consider that multiple IHT100 forms are required where IHT is due? Would HMRC agree to a concessionary position where no IHT100 forms were required where no IHT was due, to remove administration for both the taxpayer and HMRC in this situation?

Answer: Where Inheritance Tax is due multiple IHT100s would prima facie be necessary. If difficulties arise tracing the consolidated fund back to trusts A B C Dand E then I'm sure we would take a pragmatic approach probably based on some form of pro rata apportionment.

Where it is clear on values that no Inheritance Tax is due we would take a pragmatic approach and where possible not insist on a formal accounting on Forms IHT100.

5 SIPP consolidation scenario with mixture of contract and trust-based "feeder" pensions

A Retirement annuity contract 1980		
B Retirement annuity contract 1986	D consolidated into trust-based SIPP in February 2008	E discretionary trust set up with £100 in March 2008
C Trust-based personal pension 1994		

The scenario here is that X starts with 3 different pension policies, one of which is trust-based and two of which are contract-based. In February 2008, he consolidates them into a SIPP. In March 2008, he creates a discretionary trust with £100 and a letter of wishes (non-binding) is given to the trustees of the SIPP indicating X's preference that the LSDB should be paid to the discretionary trust. X then dies in March 2010 and the LSDB is paid to the discretionary trust. The question arises as to the number of settlements and nil rate bands in this scenario.

Question 5a: Does HMRC agree with the analysis that there are 3 settlements and 3 nil rate bands here? The first is pension C, with a TYA date which refers back to the 1994 date. The second is the SIPP at D, with a TYA date which refers to the date the SIPP commenced. The third is the discretionary trust at E. The pensions at A and B are not taken into account for settlement purposes as they are contract-based pensions and therefore there is no property moving between settlements at the point they are transferred to the SIPP, and there is therefore no "tracing back". Does HMRC agree with this analysis?

Answer: Confirmed. This is our current analysis for contract based schemes. Our view is that these are not settlements within s43IHTA and in that event s81 IHTA does not apply. The funds transferred from pensions A and B become settled property on their transfer into the SIPP at D.

Question 5b: New pension contributions may or may not be made into the SIPP at stage D. Does HMRC agree that, regardless of whether or not there are new pension contributions, or whether D is simply a pure consolidation exercise, this does not affect the overall number of settlements, which remains the same as in 5a, namely 3 settlements?

Answer: Confirmed.

6 Sequential transfers of trust-based pension arrangements

A trust-based pension 1988	B trust-based pension 1996	C trust-based SIPP 2008	D discretionary trust set up with £100 in March 2008

X's first pension dates back to 1988. In 1996, he established pension B using a transfer value from pension A. Then in 2008, X takes out a SIPP using the transfer value from pension B. In March 2008, he creates a discretionary trust with £100 and a letter of wishes (non-binding) is given to the trustees of the SIPP indicating X's preference that any LSDB should be paid to the discretionary trust. X then dies in March 2010 and the LSDB is paid to the discretionary trust. The question arises as to the number of settlements and nil rate bands in this scenario.

Question 6a: Assume that X made no new pension contributions after pension A, so that the move to pension B and then pension C was effectively just a change of investment wrapper. The analysis here seems to be of two settlements. One is the discretionary trust D, with its TYA relating to its initial £100 gift. There is also a second settlement. This seems to be either the SIPP, or pension A. In either case, the value would be the same, and the only difference would relate to the TYA date, as being either the date of pension A or the date of commencement of the SIPP. Does HMRC agree with the analysis that there are two settlements here, and that pension B is ignored, and if so, what is the appropriate date for the TYA as discussed above?

Answer: Agreed. Section 81 would take us back to Settlement A as setting the appropriate date for the TYA.

Question 6b: Assume now that there are new pension contributions made into pension B, whereas the move from pension B to the SIPP is simply a change of investment wrapper. Does HMRC agree that the analysis here involves 3 settlements, with TYA dates which refer to the dates of commencements of each of A, B and D?

Answer: Confirmed.

Question 6c: Assuming that new pension contributions were made at stages A, B and C, does HMRC agree that the analysis involves 4 settlements, namely A, B, C and D, each with its own TYA reference date?

Answer: Confirmed.