HANBURY WEALTH

Hanbury Wealth Product Guide

Pensions Death Benefits

2025/26 Tax Year

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What would you like to happen to the benefits from your pension plans in the event of your death?

Depending on the type of pension plans you have, it is usually possible for you to either complete a nomination form (also referred to as an 'expression of wish form') specifying what you would like to happen to your death benefits or to place your death benefits under trust.

With most occupational pension schemes the nomination form is the only option and this will also be the case with some individual pension plans such as personal pensions. The pension plan trustees or administrators have discretion over who they pay death benefits to but the nomination form makes them aware of your wishes and, in normal circumstances, they will usually follow them.

Some older plans such as retirement annuities and buy-out bonds (section 32 plans) may require that a trust wording be completed rather than a nomination form.

We have given more detail on the possible options (in terms of death benefit instructions) below.

Points to consider

In light of the new pension flexibilities for death benefits, including the potential to pass funds down through the generations via flexi-access drawdown, and the possibility of paying death benefits to a far wider range of beneficiaries, it is important to bear in mind that it may be impossible to make use of these options if your pension plan or scheme doesn't offer them.

It is important to check whether your pension arrangements can be used in the way you would like on your death. If you have pensions that can't facilitate the new freedoms, for example older pension plans that don't give your beneficiaries the option of leaving the remaining pension funds in drawdown, your beneficiaries could find that the only option available to them is annuity purchase or to take a lump sum (which may not be the most tax efficient option).

- What would you like to happen to any remaining pension fund on your death?
- Would you like your beneficiaries to have the option of the tax efficiency and flexibility of inherited drawdown?
- Is a secure fixed income from a survivor's annuity more appealing?
- Would a lump sum death benefit be better directed to a bypass trust where your chosen trustees can have the control over who benefits and when (which could include making loans)?
- Can the existing pension scheme facilitate your preferences? Not all pensions allow lump sum payments to be made to a bypass trust and not all pensions offer inherited drawdown.

- Nomination form issues:
  - Even where the pension arrangement offers all the new freedoms, it's crucial that nomination forms are kept up to date and fully reflect your wishes.
  - A death benefit nomination helps to guide the scheme trustees / administrators when exercising their discretion and they will rely on the most recent nomination form they have received. Nomination forms can normally be changed at any time.
  - The new rules around who can inherit make it even more important that nomination forms are correctly completed. If you want someone other than a dependant to inherit and would like them to have the option of inherited drawdown, you must name them on the nomination form – a lump sum can, however, be paid at the trustees' discretion to a non-dependant even if there is a surviving dependant.
  - Issues can also arise where you have completed a nomination form with instructions that the lump sum death benefit is to be paid to a bypass trust. Some nominations to a bypass trust can be made binding upon the scheme administrator, in which case the scheme administrator must follow this instruction and has no discretion to pay to anyone else – such a binding nomination can still be revoked by completing a new nomination.
  - In light of the pension freedom changes you will need to decide if a bypass trust is still the right option. Bear in mind that a lump sum paid to a trust if you were to die after age 75 is taxed at 45% initially (a 45% tax credit is then given to the beneficiary when capital is distributed to them from the trust and they can reclaim any difference between 45% and their own income tax rate).
  - From 6 April 2024, only death benefits that are taken as lump sums from funds crystallised after 5 April 2024 on death before age 75 are tested against the Lump Sum and Death Benefit Allowance – lump sums are tax free within the allowance but any excess is subject to income tax on the recipients. This issue doesn't apply where beneficiary drawdown is an option as, on death before 75, unlimited funds can pass into beneficiary drawdown and then be withdrawn tax free by the beneficiaries. This is another reason to ensure that beneficiary drawdown is available to your beneficiaries if your death benefits are likely to exceed your available Lump Sum and Death Benefit Allowance.
  - Most pensions are currently free from inheritance tax. For deaths after 5 April 2027 the government intends that most pension death benefits will form part of the deceased's estate. If left to a spouse or civil partner, the spousal exemption from inheritance tax will apply.

Types of beneficiaries

Death benefits from pension plans can now be paid to any of the following classes of beneficiary (with the exception of scheme pensions where on death of the member the scheme pension can only be paid to a 'dependant' as defined below):

- One or more dependants (which means your spouse or civil partner, your child aged under 23 (or older but dependent due to a disability), any of your financial dependants (or anyone mutually dependent on you)).

- One or more nominees - a nominee is anyone you would like to benefit who doesn't fall into the 'dependant' definition above (for example, your adult children). A nominee can be nominated by you or by the scheme administrator. If you have a surviving dependant or if you've nominated an individual or charity, the scheme administrator cannot choose a nominee instead.

- One or more successors – a successor can inherit after the previous beneficiaries have died. The successor can be nominated by either the previous dependant, nominee or successor or, in some cases, by you (via your original instructions) or the scheme administrator.

Ways to make your choices regarding death benefits

One or more of the following options may be available in relation to any particular pension plan or scheme and it is important that this be checked with the scheme or pension provider in order that the appropriate actions can be taken in relation to the death benefits.

Writing the policy under trust / nomination

With uncrystallised personal pension plans and drawdown plans you may have the option of writing the death benefits under a form of discretionary trust (often referred to as a Spousal By-pass Trust) or by completing a nomination (expression of wish) form. The only type of death benefit that can be paid to a trust is a lump sum. With a nomination form, additional options such as drawdown may be available to your beneficiaries. If you elect not to make a nomination or use a Trust, the Trustees / administrators of your pension will liaise with your estate following your death and make a decision as to who should benefit; however this may not be the outcome you had intended so it is best to consider how a nomination or trust could help.

Using an individual trust

By writing your policy under an individual trust you can ensure that, in the event of your death, the benefits are available to the trustees for distribution without unnecessary delay. By placing in trust you are ensuring that your chosen trustees have the discretion over payment of the death benefits, which might include loans to beneficiaries (which can bring added inheritance tax planning opportunities for the beneficiaries as the repayment of the loan on the beneficiary's death will reduce their own estate). It is possible that tax charges could be incurred within the trust after your death, i.e. on 10 yearly anniversaries and when funds are paid out of the trust, depending on the amounts involved.

The payment of the lump sum into the Trust will be paid free from income tax if you die before age 75 and, if paid from funds crystallised after 5 April 2024, it is within your available Lump Sum and Death Benefit Allowance but were you to die after 75 the income tax rate deducted on entering the Trust is 45%. Any beneficiary receiving a payment from the trust then receives a corresponding tax credit that they can offset against their own income tax liabilities.

Nomination into trust or to individual beneficiaries

A nomination, although not binding, ensures that, in the event of your death, the administrator takes into account your wishes as to where benefits should be paid without unnecessary delay. Nomination forms can be altered at any time prior to your death and should be revisited regularly.

A nomination form can be used to nominate that death benefits be paid into a trust on your death (lump sums only) as well as being used to nominate that benefits be paid to particular individuals. These instructions can be changed at any time. If there comes a time when it might be preferable for your death benefits to be paid to individual beneficiaries rather than into a trust, your nomination form can be altered to reflect this, i.e. After your 75th birthday when the tax rate on lump sum death benefits will be at the recipient's own income tax rate(s) rather than the 45% tax rate applicable at outset to trusts.

As a result of the pension freedoms introduced on 6 April 2015 it is possible, if the product allows, for pension funds to be left within the pension wrapper indefinitely following your death to be drawn on by subsequent generations of beneficiaries for as long as the funds last. It is therefore very important that your death benefit instructions accurately reflect your wishes and are kept up to date.

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