Pension Death Benefits and the use of Pilot Trusts

Many people have heard the expression "pilot trust" or "spousal bypass trust". Either term is commonly used in the context of members of pension schemes directing, by way of nomination, death benefits into a trust thereby enabling that scheme member, by the careful choice of trustees, to retain some control over the monies and benefit a range of persons according to their needs.

Further, where necessary, this planning means that the monies can be kept out of a specific dependant's estate for inheritance tax purposes. This is achieved by the scheme member setting up a lifetime trust for a nominal amount, say £10.00, and nominating the pension death benefits into that trust. The trust would normally lie dormant until receipt of the death benefits.

Whether or not a nomination can be made into a trust arrangement in this manner will depend upon the scheme rules, but in most circumstances the scheme rules will allow this type of arrangement.

Lump sum payments on death from a pension scheme can come from insured arrangements, commonly referred to as ‘death in service’, or the value of the pension fund itself where that fund has been built up by the member's contributions. Pension law is complex but most pension schemes do provide for a capital payment to be made on the death of a scheme member, prior to that member having taken benefits.

Many pension schemes also provide, particularly personal pension schemes, for capital payments to be made on death after the member has taken benefits, but subject to tax charges.
Where a member has taken benefits from a pension scheme which under its scheme rules allows a dependant to continue to take pension after the member's death, it is important to provide safeguards in terms of a nomination into a trust so that there is an option for the dependant to continue to take pension income payments rather than a lump sum payment where circumstances suggest this is appropriate.

Many pension nominations are in favour of a spouse and it is always therefore worth considering whether a nomination of the whole of or part of those death benefits into a trust arrangement, where spouse and children can benefit, could be more flexible and meet the family's particular circumstances.

Whilst any type of trust used for this purpose may have its own taxation regime upon which advice is required, in a majority of cases it is certainly worth looking into this type of arrangement.

Once the trust is in place, where the terms of that trust allow monies to be loaned to a beneficiary, e.g. a spouse, those loans could be made from the trust which could have the result of reducing the spouse's estate on their death as there would be a debt due to the trust from the spouse's assets.

If you are interest in looking into this arrangement in more detail then contact Dan Attfield on 01245 850000 or by e-mail at dan@affinitywills.co.uk