



Tax efficient succession planning for your Approved Retirement Fund

For further information on this topic please contact Irish Life's Life Advisory Services Team.

We advise that your client seeks professional tax and legal advice as the information given is a guideline only and does not take into account your client's particular circumstances.

In general, when assets are passed on death, the beneficiary of the asset is subject to Capital Acquisitions Tax (CAT) in the form of inheritance tax, with the spouse / civil partner exemption applying where the asset passes to a legal spouse or a registered civil partner.

This is not the case with the value of your clients Approved Retirement Fund (ARF) / Approved Minimum Retirement Fund (AMRF) / Vested Personal Retirement Savings Account (PRSA). Below is a table showing how these funds are taxed on death.

Taxation of ARF / AMRF / Vested PRSA funds on death

| Funds to | Income Tax | Inheritance Tax |
|---|--|---|
| Spouse / Civil partner's ARF | No. Subsequent withdrawals subject to PAYE. | No. Spouse / Civil partner exemption |
| Other (Including spouse or civil partner directly) | Yes. Income of deceased in year of death. Qualified Fund Manager (QFM) deducts higher rate tax under PAYE. | Yes. Taxable Inheritance (spouse / civil partner exemption applies to legal spouse or registered civil partner) |
| Child under 21 | No. | Yes. Taxable Inheritance |
| Child over 21 | Yes. Subject to 30% tax regardless of fund size. | No. Exempt |

Applies to ARF's set up post April 2000.

So, if your clients spouse or civil partner needs the value of their ARF to provide an income after death, he or she can retain the investment intact, and any subsequent drawdowns made will be liable to income tax in the normal manner.

If, however, the ARF is not required for income purposes: and your clients spouse or civil partner decides to encash it, this will be considered a distribution from the ARF and will be subject to Income Tax at **your client's** marginal rate. The QFM is obliged to deduct this tax under Section 784A Taxes Consolidation Act (TCA) 1997.

If, however, the ARF is not encashed, but just transferred into the name of your client's spouse or civil partner, the value of the ARF will be reduced every year by an 'imputed distribution'.

So, if your clients spouse or civil partner does not need the value of the deceased's ARF to generate an income, maybe there is a more tax efficient way to pass on this particular asset?

Instead of your client leaving their ARF to their legal spouse or civil partner, they could leave it's value to their children. As you can see from the table, the tax treatment of the value of the ARF will be different depending on the age of the child receiving it. A child under 21 will be subject to Inheritance Tax, whereas a child over age 21 will be subject to tax at 30%, regardless of the size of the fund. Again the QFM is obliged to deduct this tax under Section 784A TCA 1997.

While you might be familiar with the use of Section 72 life assurance policies to fund for the payment of Inheritance Tax, did you know that the income tax arising on the transfer of the value of an ARF to a child over age 21 can also be funded for using Section 72 relief?

This means that assets held within an ARF can be protected and passed on to your client's children in a tax efficient manner through the use of a Section 72 life assurance policy.

The extension of the relief under Section 72 CAT Consolidation Act 2003 to include the income tax payable by a child over 21 gives you a real opportunity to review your clients existing estate planning provision.

The 'Section 72' option referred to above is not the only solution to this problem for your clients.

It is worth noting that as an alternative to your client effecting a Section 72 life assurance contract for the benefit of their beneficiaries, if their children are old enough to effect a life assurance contract (i.e. age 18) and where they have their own independent income, there is an option for the children to fund for this tax bill themselves through the use of life assurance.

Your client's children can effect a 'life of another' life assurance contract with your client as the life assured. The child will be the policy owner and they will pay the premium themselves. In the event of the death of their parent the child will receive the full sum assured from the policy, without any tax deduction, and they can use that money to pay any inheritance tax or income tax arising on the inheritance of any assets, including an ARF.

In this short note we have given you something to think about when you are reviewing your clients 'succession plan' for their ARF / Vested PRSA. We hope we have also given you some potential solutions to the tax issues that may arise as a result of that plan.

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