Inheritance tax changes – getting prepared for April 2027

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Most unused pension funds and death benefits payable from a pension scheme will fall within a person's estate for inheritance tax purposes in respect of deaths on or after 6 April 2027. In this hot topic, we consider the key changes and what trustees should be doing now to prepare.

Background

When an individual dies, inheritance tax ("IHT") is charged on their estate where its value (together with certain lifetime transfers) exceeds a personal tax-free allowance (currently £325,000). A further allowance of up to £175,000 may apply where a main residence is left to direct descendants (ie children and grandchildren). Subject to certain exceptions, death benefits under registered pension schemes have generally not attracted IHT. But, following a change in Government policy, this will change from April 2027.

What's in scope?

Unused DC pots (including DC AVCs) and the value of any scheme assets that "may or must" be used to provide benefits on the death of the member (including a five-year guarantee lump sum or refund of contributions) will generally be subject to IHT.

Excluded benefits
Benefits **excluded** from the scope of the IHT changes include:

- death in service benefits payable from registered pension schemes
- a dependant's scheme pension (eg a pension to a spouse or child), and
- a dependant's or nominee's annuity that was purchased together with a lifetime annuity payable to the member (commonly referred to as joint life annuities).

Exemptions
The existing IHT principles providing exemptions for death benefits passing to a surviving spouse or civil partner who is a long-term UK resident, and registered charities, will be maintained.

Which schemes are affected?

The changes will apply to registered pension schemes, qualifying non-UK pension schemes, and section 615 schemes. Excepted group life schemes are **not** in scope, as they are not registered pension schemes.

Who is the "scheme administrator" for tax purposes?

The role of the pension scheme administrator for tax purposes ("PSA") is different from the role of the day-to-day administrator. The PSA is usually the trustees, but this is not always the case (eg if the trustees are non-UK resident). It is the PSA who will be responsible for dealing with the new IHT obligations.

How is HMRC helping schemes prepare?

HMRC has published a technical note providing detail about the proposed changes. It is also planning to publish a further technical note "later this summer", setting out more information about withholding notices and payment notices, as well as providing example scenarios to illustrate the new processes and addressing common queries raised by the industry. It also intends to provide further updates in future pension scheme newsletters.

Reporting and paying IHT

Personal representatives ("PRs"), who already report and pay IHT on the deceased's estate, will be primarily liable for reporting and paying IHT.

Pension beneficiaries will become jointly and severally liable for any IHT due on unused pension funds and death benefits to which they are entitled, from the point they are confirmed as the beneficiary. There are also limited circumstances where the PSA may be liable, eg where it has failed to pay any IHT due after receiving a valid payment notice (see below).

Options for paying IHT due on any death benefits

PRs can pay from the free estate	PRs or any beneficiary can direct the PSA to pay IHT (see below)	Beneficiary can take benefits in full and then pay IHT

Payment notices
PRs and beneficiaries can direct the PSA to pay IHT due on benefits held in the scheme by issuing a "payment notice", through the "pensions direct payment scheme". Certain conditions need to be met, including that the IHT is at least £1,000. Once a valid payment notice is received, the PSA has to pay the amount specified in the notice within 35 days of receipt.

Withholding notices
PRs and prospective PRs can also ask the PSA to withhold 50% of benefits payable to an individual for up to 15 months, by issuing a "withholding notice", where they have reason to believe IHT may be payable on those benefits. While a withholding notice is in place, PSAs should ensure that affected beneficiaries are able to access up to 50% of their benefits "promptly". However, no further benefits can be paid during that period where they have already received over 50% of their benefit entitlement.

Information sharing requirements

Regulations have been made setting out the information that PSAs and PRs must supply to each other, beneficiaries and HMRC after the death of a scheme member. This includes information needed for valuing the benefits, withholding notices and payment notices.

What should trustees be doing now?

+ Check whether they are the PSA.
+ Liaise with their day-to-day administrators to understand how they are preparing for the changes, including getting information sharing and IHT direct payment processes in place.
+ Ask their day-to-day administrators to check scheme rules to understand which benefits are in scope. If there are any complex benefits, ask for legal input.
+ Update scheme documents as needed (eg removing references to death benefits falling outside of a member's estate for IHT purposes).
+ Inform members of the proposed changes, eg on the scheme website or in a member newsletter.

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