Group protection briefing, Q3 2025

From April 2027, unused pension and death benefits will be subject to inheritance tax (IHT).

In this briefing, we explain the oncoming tax rules and provide key takeaways for pension scheme trustees and employers.

In the 2024 autumn Budget it was announced that from 6 April 2027, most unused pension funds will fall into an individual's estate for IHT purposes. This includes most funds paid out after death, as a lump sum, a beneficiary's drawdown or an annuity.

Currently, most pension funds lie outside the estate because they are paid at the discretion of the scheme trustees. These new rules eliminate the distinction between discretionary and non-discretionary payments, meaning IHT will be payable on the gross value of the pension funds immediately before death, and before distribution to beneficiaries. The standard rate of IHT is 40%. The principles that provide exemption for death benefits passing to a surviving spouse, a civil partner, or a registered charity will be maintained.

The underlying rationale is to prevent pension schemes being used and marketed as a tax-planning vehicle to transfer wealth, rather than for funding retirement.

It has been noted that this change won't impact most people due to the nil rate threshold of £325,000 (or £500,000 if including a family home). However, government figures estimate that in the first year, the measures will make 10,500 more estates subject to IHT, and 38,500 will pay more.

This means that many people will need to reconsider their estate planning, and may benefit from financial advice.

For pension schemes, the most welcome change to the original proposals may be that their administrators won't be liable for IHT reporting and payment. See our **previous weekly bulletin** for further information.

Death-in-service benefits will remain exempt from IHT

The Government has clarified that, despite wider reforms bringing most unused pension funds and death benefits into the scope of IHT, *death-in-service benefits* from registered pension schemes will be exempt. This decision is in response to a technical consultation following the initial announcement.

The Government has acknowledged that including these payments would create inconsistencies, particularly compared with similar benefits held outside pension arrangements.

Industry reaction has been positive, and the decision is particularly welcome given that these benefits are a lifeline for bereaved families. The exemption ensures that immediate financial support is not delayed by complex tax issues and that death-in-service arrangements continue to serve their intended purpose: providing timely support to dependants in difficult times.

Key takeaways for employers and trustees are that:

- Individuals should prepare for changes in estate-planning processes and communicate these clearly to families.
- Personal representatives – not pension schemes – will manage IHT, where applicable.
- Death-in-service benefits from registered schemes will be IHT-free, whether discretionary or non-discretionary.

Get in touch with our specialist team to discuss how group protection and complimentary services can help your organisation.

Or **find out more about our group protection services**.