

LCP's response to HMRC's consultation on introducing Inheritance Tax on unused pension funds and death benefits

15 September 2025

This document sets out LCP's response to HMRC's technical consultation on the draft legislation to bring unused pension funds and death benefits into scope of Inheritance Tax [published](#) on 21 July 2025 (the "Draft Legislation").

Who we are

LCP is a firm of financial, actuarial, and business consultants, specialising in pensions, investment, insurance, energy, health and business analytics. We have over 1,000 people in the UK, including over 180 partners.

The provision of actuarial, investment, covenant, governance, pensions administration, benefits advice, and directly related services, is our core business. About 80% of our work is advising trustees and employers on all aspects of their pension arrangements, including the application of the pensions tax regime to benefits. The remaining 20% relates to insurance consulting, energy, health and business analytics. LCP is regulated by the Financial Conduct Authority for some insurance mediation activities only and is licensed by the Institute and Faculty of Actuaries for a range of investment business activities.

Executive summary of our views

We welcome the Government's revisions to its initial proposals to reflect the feedback provided by LCP and others in the pensions industry, particularly in relation to the scope of the new Inheritance Tax (IHT) regime and the mechanism for collecting IHT on pension benefits.

The shift of responsibility for calculating and paying IHT from Pension Scheme Administrators (PSAs) to the Personal Representative (PR) will be welcomed by PSAs. However, much of the burden has simply shifted to the PR at a time when, assuming they are a family member, they may well be vulnerable having recently been bereaved. We are concerned that timescales involved remain unrealistic, with a material risk of late payment charges being incurred, often at no fault of PR, PSA or beneficiary.

Overall, we believe further clarity from HMRC in the below key areas will be essential ahead of the implementation of the changes from April 2027.

- **Scope of exemption for death in service benefits:** We are pleased with the proposal to exempt death in service lump sums from IHT. However, clarity is needed from HMRC to ensure that the final legislation matches the policy intent in this area.
- **Consistency in survivor pension treatment:** We also welcome HMRC's confirmation that survivor's rights paid from a joint life annuity are not part of a member's estate and are not in scope of IHT. Whilst this aligns the treatment of joint life annuities with dependants' scheme pensions, some inconsistencies remain between other survivors' pensions payable from money purchase arrangements, compared to dependants' scheme pensions.
- **Processing and information requirements:** We are concerned that the reporting and payment timescales for PSAs (and PRs) will be unachievable in a number of scenarios. To minimise any disruption, it is essential that the updated information sharing requirements are shared as soon as possible to allow sufficient time for the industry to review and comment on the changes and to make the necessary updates to systems and processes ahead of April 2027. We are also concerned that the reporting of information to PRs on the value of pension benefits paid to individual beneficiaries will create conflict between beneficiaries.

We have provided further details below.

Calculation and payment

PSAs are not experts in IHT and it is appropriate that they should not be expected to calculate how much IHT is due. The PR will have a fuller picture of the deceased's assets and so is much better placed to do so.

In many cases the death benefit from a pension scheme is small (for example a DC pot of less than £10,000 or a funeral grant of £1,000 or less). The benefit is also payable as a single lump sum. The beneficiaries have no right to payment in instalments, the PSA is not set up to pay in instalments and the administrative costs of making multiple payments would be disproportionate. It is therefore welcome that the 'scheme pays' mechanism only applies on a compulsory basis where the benefit is generally more than £10,000 and that PSAs can proceed with making payments without needing to wait for information or permission from the PR. It is also welcome that there is no requirement to have to withhold payment to the pension beneficiaries whilst waiting for them to make an election.

Benefits in scope

The revised policy intent is that 'death-in-service' benefits from registered pension schemes will be out of scope of IHT, regardless of whether the benefit is discretionary or not.

However, we would like clarification of the operation of proposed new section 150A(6) IHTA 1984 in relation to:

- Situations where part of the death in service benefit payable is also payable in other circumstances (eg a refund of contributions could be payable for death in deferment as well as on death in service, the latter being in addition to typically a multiple of the member's salary). How much of the death benefit meets the definition in the draft legislation of '*not payable unless the member is an active member of the scheme*'? We have set out a number of example scenarios in Appendix 1. Please could you confirm which (if any) of the benefits payable in these scenarios would be in scope of IHT?
- Whether the definition of 'active member', as cross-referenced to s151(2) FA 2004, includes (a) members of a standalone registered pension scheme providing death in service benefits only, and (b) 'employed deferred' members in a registered pension scheme which continues to provide 'death in service' benefits whilst a member remains in company employment.
- Whether the requirement for the member to be 'in employment' needs to be amended to ensure that death in service benefits paid to self-employed individuals would be out of scope of IHT, which we assume is the policy intention?

In all three cases it is not clear to us the draft legislation achieves the policy intention and, as a result, we anticipate there will be material inconsistencies in treatment by PSAs.

Death in service lump sums provide vital benefits at a time of great need and we are pleased that the Government have decided to remove these benefits from the scope of IHT. However, as we have illustrated above, it is not clear to us whether the current draft legislation fully achieves this policy intent.

Inconsistencies between survivor pensions

The response to the initial 2024 consultation clarifies that survivor benefits from joint life annuities will not form part of the member's estate for IHT purposes. We welcome this change as it aligns the treatment of dependants' scheme pensions and dependants' annuities, where a joint life annuity has been purchased prior to an individual's death. It will be welcomed by those intending to or who have already bought joint life annuities with the survivor benefit destined for an individual who is not a spouse or civil partner. It also removes the issue of how such a benefit could be valued for IHT purposes.

We understand that the associated pension asset would have been part of a member's estate prior to the purchase of the reversionary annuity. Please can you explain if the pension asset simply ceases to be part of the member's estate on the day it is purchased, or only upon death? Would the annuity purchase be a potentially exempt transfer, or is the situation more complex?

In addition, we note that other potential inconsistencies between defined benefit survivor pensions and money purchase survivor pensions remain. Is this the Government's intention? Our understanding is as follows:

- On death of an individual not in service prior to their pension benefits coming into payment (eg on death in deferment), a dependant's annuity purchased from the deceased's DC pot that is not for the benefit of the deceased's spouse or civil partner would be in scope of IHT but a dependant's scheme pension payable in the same circumstances would be out of scope of IHT.
- Where money purchase funds are used for drawdown, a dependant's annuity that is not for the benefit of the deceased's spouse or civil partner purchased following death from unused drawdown funds would be in scope of IHT, but if the money purchase funds had instead been used to purchase a joint life annuity prior to death, the survivor benefits from the joint life annuity would be out of scope.

Processing and information requirements

PSAs will be required to make payment of any IHT within three weeks of a valid "scheme pays" request from a beneficiary. We think this deadline will be unachievable in the following circumstances:

- If there are significant investments in illiquid assets which require disinvestment, which can often take significantly longer than the three-week deadline.
- Where Bank Holidays fall within the three-week period. There will also be additional strain on pension scheme administrators during holiday periods – for example around Christmas.

Provided the consequences of missing the three-week deadline remains as proposed in the consultation (the PSA becomes jointly liable for the IHT due on the pension benefit provided the pension benefit had not been paid to the beneficiary), we consider the proposal workable. However:

- There would be an issue if the PSA were to become subject to a penalty or interest on the IHT due.
- The PSA should not become jointly liable (or the notice should be considered null and void) in the event that whilst the notice was received before the benefit was paid, the process to make the payment was already in motion.
- Please can you clarify whether interest continues to accrue between the date of the 'scheme pays' election and the date of payment. If so, please can you confirm the PSA is responsible solely to pay the amount of interest specified on the election and any further interest would need to be paid by the pension beneficiaries.

HMRC have stated that PSAs must provide the value of the pension benefits to the PR within four weeks of receiving notification of the member's death. We note the draft updated information sharing regulations are yet to be published, but we have provided some initial commentary on this and further questions in Appendix 2. It is essential that the pensions industry is given sufficient time to review any new requirements, to allow time to raise comments and questions, and then make the necessary updates to systems and processes ahead of April 2027.

Deadlines for the IHT process are also much tighter than pension schemes are used to working to. IHT must be paid within six months of the end of the month of death to avoid incurring interest and penalties. Currently pension schemes have two years from being notified of a death before tax is triggered on death benefits.

In complicated cases, it can take many months for a pension scheme to be notified of a death, identify potential beneficiaries, obtain information on the nature of their relationship to the deceased and their financial position, and determine who the benefits should be paid to. In such situations late payment charges will be incurred, often at no fault of the PSA or beneficiary. It will be important to have clear guidance from HMRC to PRs on what to do in situations where the six-month deadline for submitting an IHT account is approaching, and a pension scheme has not been able to determine how benefits will be allocated.

We note that the new disclosure requirements also create an issue for how a PSA can establish whether the individual claiming to be the PR is indeed the PR. To date, common practice has been for the PSA to request a copy of the grant of probate to evidence the identity of the PR. However, such a grant is only available after an IHT account has been submitted. A new approach to establishing the identity of the PR will be needed, especially in cases where the deceased did not leave a will. We ask that HMRC brings forward proposals on how the PSA can confirm the identity of the PR prior to providing the valuation of pension assets and personal information regarding beneficiaries.

Next steps

We welcome the open and constructive way consultations have been run, and the opportunity to attend the workshops with the pensions industry.

We note that updated draft primary legislation will be required and urge HMRC to both consult on the updated draft and release the draft information sharing regulations as soon as possible to allow sufficient time for the pensions industry to be able to provide feedback on both the revised legislation and the disclosure regulations and to allow time to implement the necessary updates required to systems and processes ahead of April 2027.

We are happy for LCP to be named as a respondent to the consultation and happy for our response to be in the public domain. We are happy for you to reference our comments in any response.

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Appendix 1

Examples to help clarify the scope of the IHT exemption for death in service benefits

Please could HMRC confirm which elements of the death-in-service package are out of scope for IHT for the following examples?

Example 1: Death in service under normal retirement age

Member accruing pension in a DB scheme whilst making DC AVCs, where the death in service benefit is a lump sum of:

- a) 4 times salary, plus
- b) A refund of member contributions, plus
- c) The AVC fund value

plus a lifetime survivor pension to a financial dependant.

(Note had the member opted out of pensionable service the day before death, the death in deferment benefit would have been a lump sum of:

- a) A refund of member contributions, plus
- b) The AVC fund value

plus a lifetime survivor pension to a financial dependant and the scheme has separate rules for death in service benefits and death in deferment benefits.)

Example 2: Death in service over normal retirement age

Member accruing pension in a DB scheme, where the death in service benefit is a lump sum of the better of:

- a) 4 times salary plus a refund of member contributions; or
- b) 5 times the pension that would have been payable had they retired the day before death

plus a lifetime survivor pension to a financial dependant.

(Note had the member opted out of pensionable service the day before death and postponed drawing their benefits, the death in deferment benefit would have been a lump sum of 5 times the pension that would have been payable had they retired the day before death, plus a lifetime survivor pension to a financial dependant.

And, had the member retired the month before death, their death in retirement benefit would have been a lump sum equal to the remaining balance of the 5-year guarantee (ie 4 11/12ths times the rate of pension on the day of death plus a lifetime survivor pension to a financial dependant.)

And the death in service, death in deferment and death in retirement benefits are each payable under different rules in the scheme.

Example 3: Death in retirement

The following example highlights the need for guidance on how different types of DC arrangements (untouched funds, UFPLS, FAD) are treated for IHT purposes, especially when the member dies under age 75.

An individual under age 75 with a combination of:

- a) A DC fund that has not been touched (from which the death benefit is the fund value that can be taken as a lump sum, used to buy an annuity for a survivor or put into a drawdown arrangement).
- b) A DC fund from which they have taken 50% as an UFPLS but 50% remains (from which the death benefits are the same as a)).

- c) A DC fund they have put into FAD, having taken a 25% PCLS (from which the death benefits are the same as a) and b)).
- d) A DB scheme pension from which is payable a £250 lump sum funeral grant and a lifetime survivors' pension to a financial dependant.

Example 4: Death where member has drawn some benefits but also still accruing

An individual with a DC fund who has taken their tax-free lump sum (and so crystallised some of the benefits) but remains employed and both they and their employer are continuing to pay DC contributions building up further uncrystallised benefits. On death, the scheme provides a lump sum of:

- a) 4 times salary, plus
- b) A return of the uncrystallised DC fund, plus
- c) A return of the unused crystallised DC fund.

This scenario raises questions about how crystallised vs uncrystallised funds are treated when the member is still actively contributing. We seek confirmation on whether the entire benefit is considered out of scope due to ongoing employment.

Example 5: Definition of “death in service”

An individual is a member of a life assurance only scheme (registered as pension scheme with HMRC) but is not accruing a pension – their only potential benefit is a lump sum on death in service.

An individual is still in employment but no longer actively at work due to ill-health or on leave.

An individual is not an employee, eg a partner or member of a limited liability partnership.

Appendix 2

Processing and information requirements

In many cases pension schemes are not notified of a member's death by the PR but by other sources, such as the deceased's spouse or a tracing agency. On such notification the pension scheme will not know who the PR is. Please confirm the intention that the four-week deadline will start from the date the PR contacts the PSA and the PSA has confirmation that the individual is the PR, not simply notification of the member's death or initial contact with an individual who it is not clear is the PR?

In some instances, the value of the benefits payable will depend on the nature of the beneficiary, which may not be established at this stage (eg in some schemes the benefit to a spouse is different from that to a non-spouse). Please confirm whether the PSA should provide details of how the value varies depending on the relationship of the beneficiaries to the deceased?

The below examples explore timing mismatches between PR actions and PSA decisions. We recommend HMRC clarify how refunds are handled, whether interest is payable, and what obligations will apply to PSAs to inform beneficiaries of the "scheme pays" option.

Example 6(A)

The PR settles the IHT on the whole estate and pension benefits before the PSA has determined the beneficiaries and before the '6 month' deadline (ie so the PR can obtain probate and distribute the non-pensions assets). In this example the PSA determines the pension assets will be paid to non-spouse beneficiaries.

Please can you confirm whether it is HMRCs intention that:

- PSAs would be required to issue HMRCs guidance on "scheme pays", and if elected for the PSA to pay the net amount to the beneficiary and pay the IHT direct to HMRC – this would not be subject to IHT interest or penalties.
- HMRC would then process a refund to the PR who would then distribute the refund to the non-pension beneficiaries – as above this would not include interest.

Example 6(B)

Assuming the same scenario as 6(A) but the PSA determines the pension assets will be paid to an exempt spouse.

Please can you confirm whether it is HMRCs intention that HMRC would process a refund of IHT to the PR, which would include interest, who would then distribute the refund to the non-pension beneficiaries?

Example 6(C)

The PR settles the IHT on the non-pensions estate and distributes the balance without any knowledge of whether the pension beneficiaries have paid the IHT due on the pension benefit nor if they have elected for "scheme pays".

Please can you confirm whether it is HMRCs intention that the PR will be jointly liable with the pension beneficiaries for the IHT on the pension benefit and could be pursued by HMRC for recovery?

Example 6(D)

The PR settles the IHT on the non-pensions estate and distributes the balance having been informed by the pension beneficiaries they have paid the IHT due on the pension benefit.

Please can you confirm whether it is HMRCs intention that the PR will be jointly liable with the pension beneficiaries for the IHT on the pension benefit and could be pursued by HMRC for recovery if it transpires that the pension beneficiaries had not paid the IHT due on the pension benefit after all?

Example 6(E)

The PR settles the IHT on the non-pensions estate and distributes the balance having been informed by the pension beneficiaries they have elected for “scheme pays” for the IHT due on the pension benefit.

Please can you confirm whether it is HMRCs intention that the PR will be jointly liable with the pension beneficiaries for the IHT on the pension benefit and could be pursued by HMRC for recovery if the PR does not obtain confirmation from the PSA that they have received a valid “scheme pays” election / paid the IHT before distributing the non-pension estate?

Guidance

We suggest it would be helpful if HMRC could provide clear guidance to PRs on what you expect them to do in the following circumstances:

- 1.1. They believe the deceased may have had an entitlement to a pension but cannot find any details.
- 1.2. They have asked the PSA for a valuation of the pension benefit but the PSA has not replied and the deadline for submitting an IHT account is getting close.
- 1.3. They have obtained a valuation of the pension benefit but the PSA has not yet been able to confirm the split between exempt and non-exempt beneficiaries and the deadline for submitting an IHT account is getting close.
- 1.4. The PSA has informed the PR of who is to receive the pension benefit but the beneficiary has not yet stated whether they will use “scheme pays” and the deadline for submitting an IHT account is getting close.
- 1.5. The pension beneficiary has informed the PR that they have elected for “scheme pays” but the PSA has not yet confirmed they have paid the tax and the deadline for submitting an IHT account is within three weeks of the pension beneficiary’s election.