OCTOBER 2026

SPOTLIGHT ON:

Pensions and inheritance tax: Preparing for the April 2027 changes

Heslops
Chartered Accountants

WWW.HESLOPS-THATCHAM.CO.UK
ENQUIRIES@HESLOPS-THATCHAM.CO.UK
01635 868202

WHY YOUR PENSION CAN NO LONGER SIT OUTSIDE YOUR ESTATE PLAN

Inheritance Tax, or IHT, is charged on the value of your estate above certain thresholds when you die, normally at 40%. Until now, most private pensions have sat outside that calculation altogether: money left unused in a defined contribution pension could generally pass to your chosen beneficiaries free of Inheritance Tax, however large the fund or your wider estate.

From 6 April 2027, that changes. Following confirmation at the Autumn Budget 2025, and legislation that has already received Royal Assent as the Finance Act 2026, most unused pension funds and lump sum death benefits will be added to the value of your estate for Inheritance Tax, and personal representatives, not pension providers, will be responsible for reporting and paying any tax due. The timing is important because Inheritance Tax thresholds are frozen for years to come, and because estate plans, pension nominations and wills built around the old rules may no longer achieve what you intended.

HMRC's own analysis estimates that thousands of estates will pay Inheritance Tax for the first time as a direct result. Inheritance Tax receipts already reached a record £8.5 billion in the 2025/26 tax year, and this change is expected to push that figure higher still.

KEY TAKEAWAYS

- From 6 April 2027, most unused pension funds and lump sum death benefits will normally count towards your estate for Inheritance Tax.
- This is now law under the Finance Act 2026, not a proposal – only the April 2027 start date is still to come.
- Personal representatives, not pension providers, will be responsible for reporting and paying the tax.
- Death-in-service benefits, and anything left to a spouse, civil partner or charity, remain outside the charge.
- Nominations, wills, retirement income plans and life cover may all be worth reviewing before April 2027.

WHAT'S CHANGING FROM APRIL 2027

From 6 April 2027, most unused pension funds and lump sum death benefits will count towards the value of your estate for Inheritance Tax. This ends a long-standing position under which pensions generally sat outside a person's estate, regardless of how much was left unused at death.

The change was first announced at the Autumn Budget on 30 October 2024, refined through a technical consultation with the pensions industry, and confirmed in further detail at the Autumn Budget on 26 November 2025. It is no longer a proposal: the core legislation is now in force as the Finance Act 2026, which received Royal Assent on 18 March 2026. Only the effective date – deaths on or after 6 April 2027 – is still to come, which gives a limited but useful window to review your position.

WHY PENSIONS ARE BEING BROUGHT INTO THE ESTATE

The government's stated aim is to stop pensions being used mainly as a way to pass on wealth, rather than to fund retirement. In its policy paper, HMRC pointed to pension freedoms introduced in 2015 and the later removal of the lifetime allowance, which together made it possible to build up a large pension fund, draw on other assets to live on, and pass the untouched pension to the next generation free of Inheritance Tax.

The government also wanted to remove an inconsistency: some pension schemes, including the NHS and judicial schemes, were already counted as part of an estate for Inheritance Tax, while most private and workplace schemes were not. Whatever your view of the reasoning,

the practical point is the same: pensions are being pulled firmly into mainstream estate planning, alongside property, savings and investments.

WHICH PENSIONS DOES THIS AFFECT?

The new rules mainly affect defined contribution pensions – personal pensions, SIPPs and most workplace pensions – where money remains unused when you die.

This can include:

- **Uncrystallised funds:** money you have not yet drawn on at all.
- **Drawdown funds:** money moved into drawdown but not yet withdrawn.
- **Most lump sum death benefits:** payable at the scheme's discretion or otherwise.

Defined benefit, or final salary, pensions are generally less affected, since most do not have an unused fund in the same sense – dependants typically receive a fixed ongoing income rather than a pot that can be left to anyone.

Annuities are treated differently depending on how they are set up: a joint-life annuity that simply continues to pay an income to your spouse or civil partner after your death is not affected by these changes, though other annuity structures may need checking individually.

WHAT STAYS OUTSIDE THE NEW RULES?

Some of the most significant pension benefits are specifically excluded from the charge. These include:

- **Death-in-service lump sums:** paid from a registered pension scheme when someone dies while still employed, whether the scheme is discretionary or not.
- **Dependants' scheme pensions:** an ongoing income paid to a dependant under a defined benefit or collective money purchase arrangement.
- **Transfers to a spouse or civil partner:** the existing spouse and civil partner exemption applies in full to pension wealth, exactly as it does to other assets.
- **Gifts to charity:** pension death benefits left to a registered charity also remain exempt.

For many couples, the first death may therefore see little practical change, since pension wealth left to a surviving spouse or civil partner stays outside Inheritance Tax. The bigger impact tends to fall on the second death, or wherever a pension is left directly to children, grandchildren or other beneficiaries.

PERSONAL REPRESENTATIVES TAKE ON THE REPORTING AND PAYING

Responsibility for reporting and paying any Inheritance Tax due on pension wealth sits with personal representatives – the executors or administrators dealing with an estate – rather than with pension providers.

This is a genuine change of direction. The original 2024 proposal was for pension scheme administrators to handle this. Following industry consultation, the government confirmed in July 2025 that personal representatives would take on the role instead, folding pension wealth into the normal probate and Inheritance Tax reporting process. Pension beneficiaries are also jointly and severally liable for tax on the pension wealth they receive, so HMRC can, in principle, pursue them directly if it is not paid.

To help fund the bill, a personal representative who reasonably expects Inheritance Tax to be due can direct a pension scheme to withhold up to 50% of the taxable death benefits, for up to 15 months from the date of death, and pay that amount towards the tax before releasing the balance to beneficiaries. Once HMRC issues a clearance certificate, personal representatives are normally protected from further liability on any pension discovered later, provided they made reasonable efforts to find it. Given this expanded role, choosing your executors carefully, and giving them a full list of your pensions, matters more than it used to.

FROZEN THRESHOLDS MEAN MORE ESTATES ARE EXPOSED

The pension change lands on top of Inheritance Tax thresholds that are already frozen for years to come, so its practical impact is larger than the headline rate suggests. The nil-rate band has stood at £325,000 since 2009, and the residence nil-rate band at £175,000, tapering away once an estate exceeds £2 million. Both were already frozen to April 2030, and the Autumn Budget 2025 extended that freeze by a further year, to April 2031, alongside the taper threshold.

Threshold	Amount	Frozen until
Nil-rate band	£325,000	5 April 2031
Residence nil-rate band	£175,000	5 April 2031
Residence nil-rate band taper	£2,000,000	5 April 2031

HMRC's own analysis, published alongside the Autumn Budget 2025 and certified by the Office for Budget Responsibility, estimates that of around 213,000 estates expected to hold inheritable pension wealth in 2027/28, some 10,500 will have an Inheritance Tax bill for the first time, and a further 38,500 will pay more than they otherwise would, with the average bill rising by around £34,000 where pension assets are included (HMRC policy paper, "Inheritance Tax – unused pension funds and death benefits," published 26 November 2025). The same measure is forecast to raise an additional £710 million in 2027/28, rising to £1,665 million a year by 2030/31.

A WORKED EXAMPLE: WHAT A PENSION COULD COST YOUR ESTATE

Suppose your estate, including your home and savings, already uses up your available nil-rate and residence nil-rate bands. You also hold a SIPP worth £150,000 that remains unused when you die, left to your adult son.

Under the current rules, that £150,000 passes to him free of Inheritance Tax. From 6 April 2027, it is added to your estate instead. Taxed at 40%, that produces a bill of £60,000, leaving him with £90,000 rather than the full £150,000.

This example assumes the whole pension falls within the taxable part of your estate. If you have unused nil-rate band or residence nil-rate band available, part or all of the pension could still pass free of tax, so the impact depends heavily on the rest of your estate, not the pension in isolation.

COULD YOUR PENSION BE TAXED TWICE?

In some circumstances, yes – the same pension can attract both Inheritance Tax and income tax, though not necessarily on the same amount at the same time.

Whether income tax is due on withdrawal depends on your age at death, a rule that is not changing. If you die before 75, your beneficiary can normally draw the pension down free of income tax, provided funds are paid out within two years of the provider being notified. If you die at 75 or over, your beneficiary usually pays income tax on withdrawals at their own marginal rate, exactly as now. What changes from April 2027 is that Inheritance Tax may also be due first, on top.

Returning to the £150,000 example, suppose you die at 78. Inheritance Tax of £60,000 is due first, leaving £90,000. If your son is a higher-rate taxpayer and draws that £90,000 as income, he could pay a further £36,000 in income tax, leaving him with £54,000 – a combined tax charge of around 64% of the original fund. This compounding effect is one reason many advisers are revisiting whether pension wealth should be left untouched for as long as possible.

DO YOUR NOMINATIONS AND WILL STILL MAKE SENSE?

Not necessarily, so this is worth checking rather than assuming. Most defined contribution pensions rely on an expression of wish form: you tell the provider who you would like to benefit, and the scheme's trustees usually, though are not legally bound to, follow it.

Some families have deliberately left pensions to children or grandchildren rather than a spouse, precisely because it avoided Inheritance Tax. Under the new rules, that choice can produce a larger tax bill than expected, and shift more of the family's overall tax burden onto the beneficiaries who receive the pension. Worth reviewing alongside your nominations:

- **Your will:** does it still reflect your intentions now that pension wealth may form part of your taxable estate?
- **Life cover:** would a policy written in trust help meet a future Inheritance Tax bill without forcing beneficiaries to sell other assets quickly?
- **Your executors:** do they know about every pension you hold, and are they equipped for a more demanding role?

SHOULD YOU STOP CONTRIBUTING TO A PENSION?

Generally, no. The case for pension saving during your working life is largely unaffected by this change. Income tax relief on contributions, employer contributions and tax-free growth within the pension remain as they are, and the 2026/27 annual allowance stays at £60,000, tapering to a minimum of £10,000 for higher earners with income above certain thresholds.

The change from April 2027 affects what is left unused at death, not what you pay in or draw for your own retirement. The more useful question to work through now is less "should I keep contributing" and more "how much of this should I plan to spend during my lifetime."

RETHINKING THE ORDER YOU DRAW DOWN RETIREMENT INCOME

Many retirees have followed a "spend other assets first, preserve the pension" strategy, and that may be worth revisiting. Because pensions previously sat outside the estate, it often made sense to draw on ISAs, savings or investment income first, and leave pension funds untouched for as long as possible, both to keep growing tax-efficiently and to pass down free of Inheritance Tax.

From April 2027, that second advantage disappears for funds left unused at death. For some people, it may make more sense to draw more from a pension during retirement and preserve other assets for beneficiaries instead. There is no single right answer: the best order depends on your income needs, health, other assets and family circumstances. Decisions about how and when to draw your pension count as regulated financial advice, so these are best worked through with your financial adviser alongside a review of the tax position with us.

GIFTING AND OTHER PLANNING OPTIONS REMAIN AVAILABLE

The normal Inheritance Tax gifting rules have not changed, and can still reduce your family's overall exposure. The annual £3,000 gift exemption, small gift allowance, wedding gifts and gifts made out of normal income all remain available, as does the seven-year rule for larger gifts, with taper relief if you die between three and seven years after making one.

From 6 April 2026, the £2.5 million allowance for the 100% rate of agricultural and business property relief also became transferable between spouses and civil partners, following further changes confirmed after the Autumn Budget 2025 – worth checking if your estate includes business or farming assets. Bringing pension wealth into the estate makes an overall gifting and estate-planning strategy more useful, not less, though gifting directly from an unused pension is not usually straightforward, since funds generally need to be drawn down, and any income tax paid, before they can be gifted onward.

> ***The annual £3,000 gift exemption, small gift allowance, wedding gifts and gifts made out of normal income all remain available, as does the seven-year rule for larger gifts***

A DIFFERENT POSITION FOR SCOTLAND, WALES AND NORTHERN IRELAND

Inheritance Tax, including this pension change, applies in the same way across the whole of the UK. Unlike income tax, Inheritance Tax is not devolved, so the nil-rate band, residence nil-rate band and the new pension rules work identically whether you live in England, Scotland, Wales or Northern Ireland.

Where the position can differ is on the income tax side of the double taxation point discussed above. Scottish taxpayers pay income tax on non-savings income under separate Scottish rates and bands, including a top rate of 48%, compared with the 45% additional rate elsewhere in the UK. This means the income tax due on a pension drawdown by a Scottish-resident beneficiary can differ from the rest of the UK, even though the Inheritance Tax treatment is the same.

CLOSING COMMENT

From 6 April 2027, most unused pension funds and death benefits will, for the first time, generally form part of your estate for Inheritance Tax – a change that is now settled law rather than a proposal. Frozen thresholds mean more families than ever are likely to be affected, and the interaction with income tax means some pension wealth could face a combined tax charge from two directions.

The main risk is inaction. Nominations, wills and retirement plans built around the old rules may no longer achieve what you intended, and personal representatives now carry more responsibility for getting the reporting right.

If you hold a defined contribution pension and have not reviewed your estate plan since these changes were confirmed, contact us before April 2027 so we can check how the new rules affect you and your family.

Heslops
Chartered Accountants

1 High Street, Thatcham, Berkshire, RG19 3JG