

Understanding the New Pension and IHT Rules from April 2027

What Is Changing and Why It Matters

For years, pensions have enjoyed a special status when it comes to inheritance tax. Most people could pass on their pension pot to loved ones without worrying about the 40% charge that applies to other assets. That is about to change. From April 2027, the government is bringing unused pension funds into the inheritance tax net, and the shift will affect how families plan their estates.

If you have a defined contribution pension or a defined benefit pension, the new rules will touch you differently. The changes are part of a broader move to align pension treatment with other savings and investments. The goal is to close what some saw as a loophole, but the practical effect is that many more estates will need to consider pension and IHT rules when organising their affairs.

The Basics of the April 2027 Change

Currently, most pension death benefits are paid free of inheritance tax. If you die before age 75, your beneficiaries can usually take the money as a lump sum or drawdown without paying income tax. After 75, the money is subject to income tax in the beneficiary's hands, but not inheritance tax. That arrangement changes in April 2027.

From that date, any unused pension funds that form part of your estate will count towards your inheritance tax threshold. The threshold, often called the nil-rate band, is currently £325,000. There is also the residence nil-rate band, which adds an extra £175,000 if you leave your home to direct descendants. These bands are frozen until 2030, so more estates will cross the threshold as property prices and pension values grow.

The change means that if your total estate, including your pension, exceeds the available nil-rate bands, the excess will be taxed at 40%. For example, if you have a £500,000 pension pot and other assets worth £300,000, your estate will be £800,000. After applying the nil-rate bands (assuming you qualify for the residence nil-rate band), the taxable amount could be around £300,000, leading to a tax bill of £120,000. That is a significant sum that your beneficiaries would otherwise have received tax-free.



How Different Pensions Are Affected

The rules apply to both defined contribution and defined benefit schemes, but the mechanics differ. A defined contribution pension is a pot of money built from your contributions and investment growth. You can usually access it from age 55 (rising to 57 in 2028) and draw income as and when you need it. The entire remaining pot will be included in your estate for IHT purposes.

A defined benefit pension, often called a final salary scheme, is different. It pays a guaranteed income for life, and on death it may provide a spouse's or dependent's pension. The value of that ongoing income stream may also be counted as part of your estate, though the calculation is more complex. HMRC will use a formula based on the pension's capital value, which could be several times the annual income.

If you have already started pension drawdown, the rules still apply to any funds left in your drawdown account. If you have taken your pension commencement lump sum, that money is already in your bank account and is treated like any other cash for IHT purposes. The new rules focus on what remains inside the pension wrapper.

Strategies to Consider Before 2027

The good news is that you still have time. The April 2027 deadline gives you a window to review your estate planning and make adjustments. One of the most straightforward steps is to review your pension nominations. A pension nomination tells the pension provider who should receive your death benefits. Updating it can ensure that the right people benefit, but it does not change the IHT position.

Another option is to consider placing your pension death benefits into a discretionary trust. A discretionary trust gives the trustees the power to decide who benefits and when. This can be useful if you want to control how your pension is used after your death, but it does not automatically avoid IHT. The trust itself may be subject to its own tax rules, so professional advice is essential.

Some people may choose to spend down their pension more aggressively during retirement, especially if they expect their estate to exceed the nil-rate band. Others may look at gifting money to family during their lifetime. Regular gifts of up to £3,000 per tax year are exempt from IHT, and larger gifts can become exempt if you survive seven years. These strategies require careful thought, because they affect your own financial security.

Practical Steps for Beneficiaries

If you are a beneficiary of a pension, the new rules will affect what you receive. Currently, if the deceased died before 75, you can take the money as a lump sum or transfer it into your own pension drawdown without an immediate tax charge. After April 2027, any inheritance tax due will be deducted before the money reaches you.



If the deceased died after 75, you will also face income tax on the withdrawal, because the pension is treated as income in your hands. The interaction between inheritance tax and income tax can feel like a double hit, although the IHT is paid from the estate before distribution. You should consider whether to take the money as a lump sum or as regular income, as this affects your overall tax position.

It is also worth remembering that the inheritance tax threshold applies to the estate as a whole, not to each pension separately. If you are dealing with multiple pensions, the total value counts towards the threshold. That means even a modest pension pot could push an estate over the limit when combined with a house and other savings.

Why Professional Advice Matters

The changes to [pension and IHT rules](#) are not straightforward. There are many moving parts, from the valuation of defined benefit pensions to the treatment of lump sums and drawdown income. A financial adviser can help you model different scenarios and decide what works best for your family.

Advisers can also help you coordinate your pension with other aspects of your estate plan. For example, you might use your pension to fund a gift to charity, which is exempt from IHT. Or you might decide to take more income from your pension and leave other assets, like an ISA, to your heirs. Each choice has trade-offs, and the right approach depends on your circumstances.

HMRC has published guidance, but it is dense and often changes. Working with a professional who understands the nuances of pension taxation can save your family from an unexpected tax bill. It also gives you peace of mind that your wishes will be carried out as efficiently as possible.

Looking Ahead

April 2027 is not far away. The new rules will apply to deaths occurring on or after that date, so there is no grandfathering for pensions built up before the change. That means everyone with a pension should start thinking about the implications now.

WILL MY PENSION BE TAXED ON DEATH?

What the April 2027 IHT changes mean for you



For many people, the key question is whether their estate will exceed the inheritance tax threshold. If it will, the new rules could reduce what your beneficiaries receive. If your estate is well below the threshold, the change may have little impact. But given that the threshold is frozen and property values have risen, more estates are likely to be affected than you might think.

The shift also raises broader questions about how we save for retirement. Pensions have long been promoted as a tax-efficient way to pass on wealth. That advantage is being eroded. It may still make sense to contribute to a pension for the upfront tax relief, but you should weigh the future IHT liability against other savings options.

Ultimately, the new pension and IHT rules are a reminder that estate planning is not a one-time task. It needs to be reviewed regularly, especially when tax legislation changes. Whether you are still building your pension pot or already drawing an income, taking time to understand the rules and seek advice can make a real difference to the legacy you leave.