Waymark financial

YOUR GUIDE TO

THE NEW INHERITANCE TAX AND PENSION RULES FROM 2027

What's changing, how it could affect you, and what to do now

In a shake-up to Inheritance Tax (IHT) rules, your pension could become part of your estate from 6 April 2027. This may mean the tax bill your estate needs to pay when you die could be significantly higher and affect what you leave behind for your loved ones.

The changes could have implications for your estate and retirement plans. So, you might benefit from making adjustments to reflect the incoming rules.

This guide explains why you may be affected by the new IHT rules and how you might manage your estate's IHT liability. If you have any questions about IHT or your overall financial plan, please get in touch.

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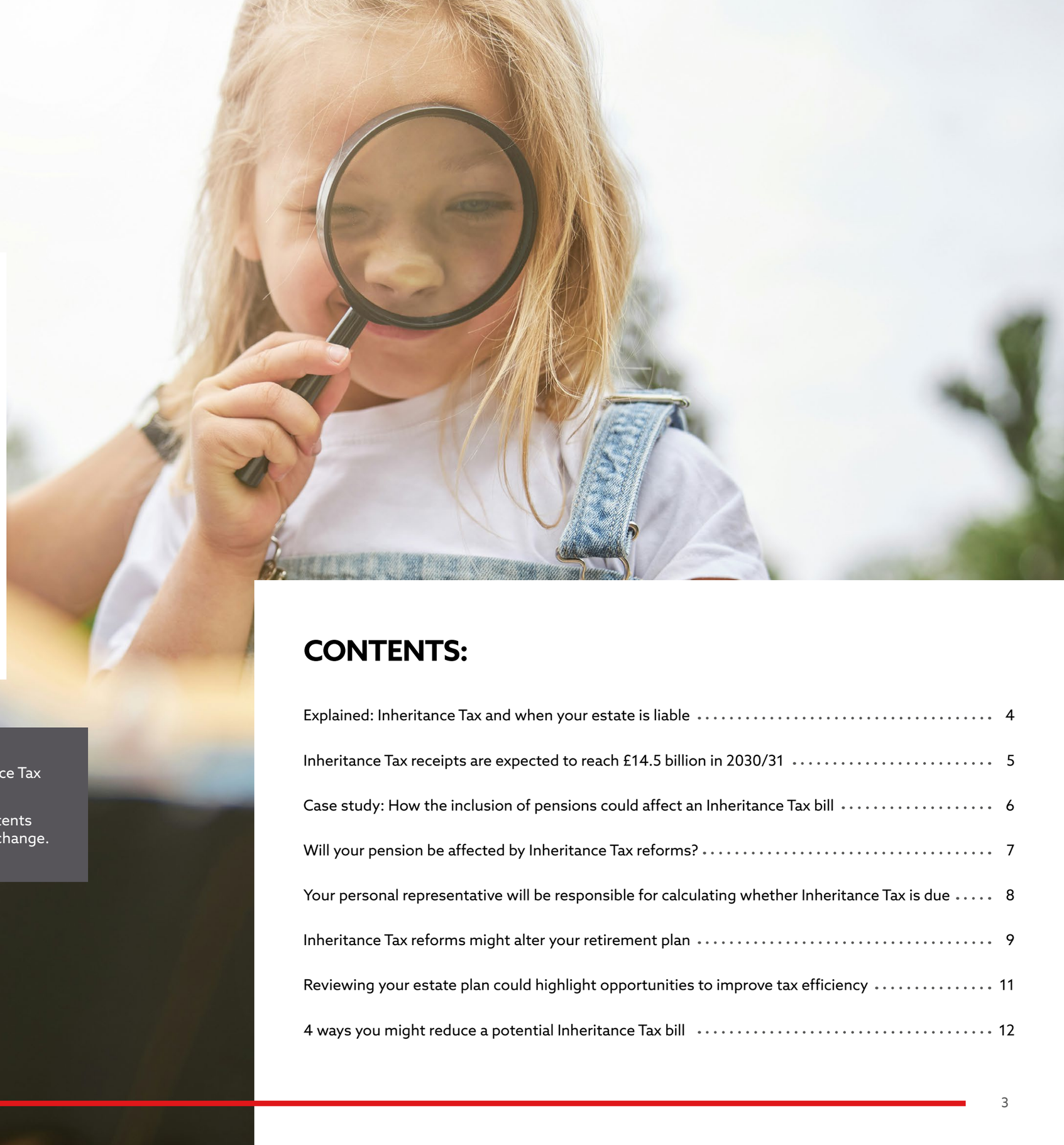

Please note: The Financial Conduct Authority does not regulate Inheritance Tax planning or estate planning.

Please do not act based on anything you might read in this guide. All contents are based on our understanding of HMRC legislation, which is subject to change.

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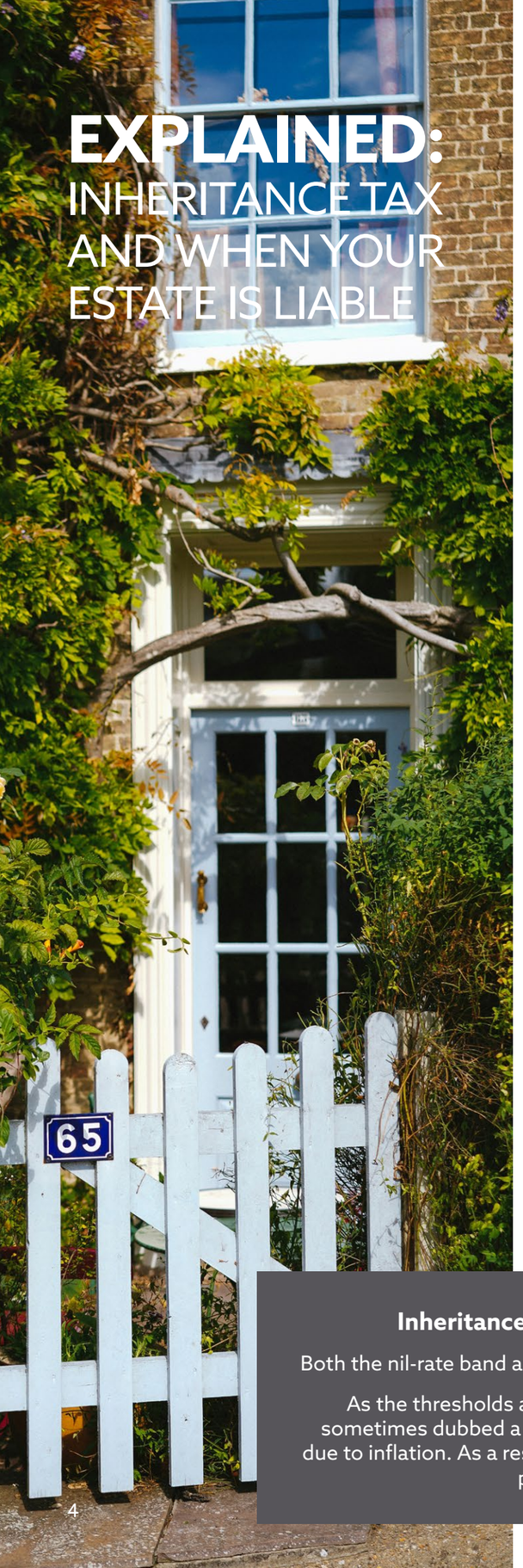


EXPLAINED: INHERITANCE TAX AND WHEN YOUR ESTATE IS LIABLE

IHT is a tax that your estate may pay when you pass away if the total value of your estate exceeds certain thresholds. In 2026/27, the standard rate of IHT is 40%, which could considerably reduce the inheritance your beneficiaries receive.

To understand if your estate could be liable for IHT, there are two important thresholds to be aware of:

1

Nil-rate band

If the total value of your estate falls below the nil-rate band, it will not be liable for IHT. In 2026/27, this is **£325,000**.

2

Residence nil-rate band

If you leave your main residence to a direct descendant, you may also be able to utilise the residence nil-rate band, which is **£175,000** in 2026/27. If your entire estate is valued at more than £2 million, the residence nil-rate band typically tapers by £1 for every £2 that your estate exceeds this threshold.

As a result, you could leave up to £500,000 to beneficiaries before you need to consider IHT.

Notably, assets you leave to a spouse or civil partner are not subject to IHT, and you can also pass on your unused allowances to them. When planning as a couple, you may be able to leave up to £1 million to beneficiaries before IHT is applied.

So, what makes up your estate?

Your estate consists of all your assets, such as property, investments, and personal possessions, less any liabilities. Crucially, pensions are currently excluded from your estate when calculating IHT, but this will change from 6 April 2027.

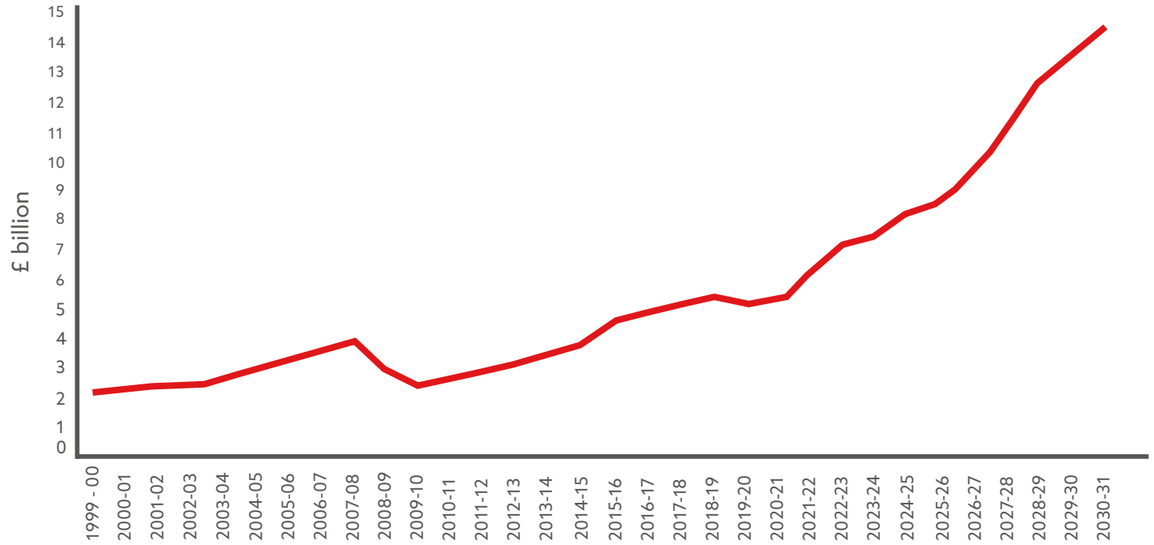
Inheritance Tax thresholds are frozen until 2031

Both the nil-rate band and residence nil-rate band are frozen until 6 April 2031.

As the thresholds aren't increasing in line with inflation, the freeze is sometimes dubbed a "stealth tax". Over time, the value of assets may rise due to inflation. As a result, even though the IHT rate isn't rising, your estate's potential IHT bill could increase.

INHERITANCE TAX RECEIPTS ARE EXPECTED TO REACH **£14.5 BILLION** IN 2030/31

Around 1 in 20 estates pay IHT. The forecast from the Office for Budget Responsibility (9 February 2026) shows how IHT reforms will lead to higher bills and more estates becoming liable for the tax.



Source: The Office for Budget Responsibility

In 2026/27, IHT receipts are expected to total **£9.5 billion**. By the end of the forecasting period in 2030/31, this figure rises to **£14.5 billion**.

The government (26 November 2025) expects that including pensions in IHT calculations will lead to an additional 10,500 estates becoming liable for the tax in 2027/28. Approximately 38,500 estates will also pay more IHT due to the reforms. The average increase is expected to be around £34,000.

The inclusion of your pension might push the value of your estate above or closer to the IHT thresholds.

According to PensionBee (24 January 2025), the median pension value of 55- to 64-year-olds with a private pension is £189,700. As a result, your pension could use up a significant proportion of your available allowances.

It's also important to consider how the value of your assets, including your pension, might change over the long term. While the IHT threshold might seem distant now, that may not be the case in the future, and your estate could unexpectedly become liable.

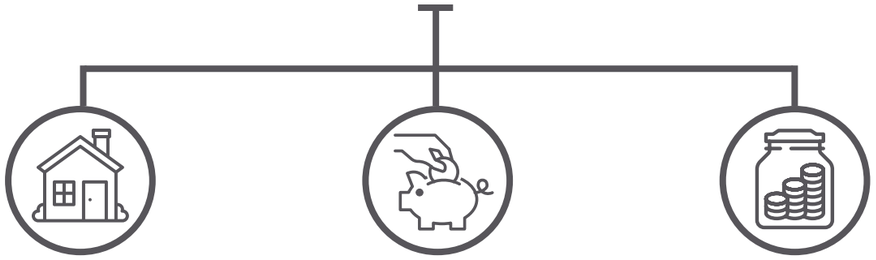
CASE STUDY:

HOW THE INCLUSION OF PENSIONS COULD AFFECT AN INHERITANCE TAX BILL

Imagine you plan to leave your entire estate to your child, and it's valued at

£800,000

Your assets are made up of:



£250,000
in property
(your main home)

£200,000
in your pension

£350,000
held in other assets
(investments, savings, and personal possessions)

As you will be leaving your main home to your child, you can make use of both the **nil-rate band** and the **residence nil-rate band**.

This allows you to pass on

£500,000

before IHT is applied.

In 2026/27, your pension is excluded from IHT calculations. As a result, only **£100,000** of your estate would be liable for IHT, leading to a bill of **£40,000**.

EXCLUDED

However, from 6 April 2027, your pension would be included, and **£300,000** of your estate would be exposed to IHT. If you passed away after the IHT reforms, the potential bill would rise to **£120,000**.

WILL YOUR PENSION BE AFFECTED BY INHERITANCE TAX REFORMS?

The new IHT reforms will not usually affect your estate's IHT liability if you leave your pension to your spouse or civil partner, who can typically inherit your entire estate without an IHT bill.

From 6 April 2027, most pensions will be included in your estate for IHT purposes. The legislation will affect most defined contribution pensions and death benefits.

A defined contribution pension means you're paying into a pot from which you can draw an income when you reach pension age (55 rising to 57 in 2028). Under current rules, passing on a defined contribution pension can be tax-efficient. However, from 2027/28, the amount remaining in your pension is likely to be included in IHT calculations.

In most cases, the following death benefits will also be included in your estate for IHT purposes:

- Lump sum death benefits paid from unused pension funds, drawdown pension funds, or pension annuity contracts
- Beneficiary's drawdown pension
- Beneficiary's pension annuity
- Payments made under a continuing guaranteed period from a pension annuity.

Some death benefits fall outside the scope of IHT reforms, including dependants' scheme pensions and dependants' annuities that are set up at the same time as your annuity.

If you have a defined benefit pension, your pension won't be affected by the IHT reforms. A defined benefit pension, also known as a final salary pension, provides a regular income from your pension provider from when you reach the pension age of your scheme until you pass away. As such, you cannot leave unused pension funds to your beneficiaries.

In addition, most death-in-service benefits will be excluded from IHT calculations. For example, if your employer provides a group life policy, your beneficiaries would typically receive between two and four times your annual salary as a lump sum if you die while still employed. In most cases, this lump sum will not be included in your estate.

If you're unsure whether your pension will be affected by the IHT reforms, we're here to help.

YOUR PERSONAL REPRESENTATIVE WILL BE RESPONSIBLE FOR CALCULATING WHETHER INHERITANCE TAX IS DUE

In your will, you can name an executor who will be responsible for managing and distributing your estate. They will need to gather information about the value of your assets, including your pension.

If you do not name an executor, the court will appoint an administrator to act as your personal representative.

Your personal representative will need to inform the pension scheme when you pass away. The pension scheme must then provide the value of the pension at the date of death, which will be used when calculating IHT, even if the value rises or falls during the probate process.

Government guidance (11 May 2026) states that personal representatives should take "reasonable steps" to identify any pension that might be subject to IHT. This may include checking the deceased's papers, records, and bank accounts, as well as speaking to relatives, beneficiaries, and financial advisers.

The information about your pension will be added to the details of your other assets to calculate whether your estate is liable for IHT. If your pension is subject to IHT and the bill is more than £1,000, your beneficiaries may be able to ask the pension scheme to pay it.

However, for some personal representatives, it might be challenging to find all the pensions, particularly if the deceased wasn't drawing an income from them or has "lost" the savings themselves. Indeed, in 2024, the Pensions Policy Institute (24 October 2024) estimated that there were 3.3 million lost pensions totalling £31.1 billion.

As a result, personal representatives might identify a pension after an IHT account has been submitted. They'd need to amend the account, and this could affect the inheritance your beneficiaries receive.

Keeping the details of all your pensions in one place could make the process as smooth as possible for your personal representative. As your financial adviser, we could also support your personal representative and provide information about your assets.

INHERITANCE TAX REFORMS MIGHT ALTER YOUR RETIREMENT PLAN

As pensions have traditionally offered a tax-efficient way to pass on wealth, your retirement plan may reflect this. For example, you might have planned to deplete other assets before using your pension to reduce a potential IHT bill.

In light of the IHT changes, you could benefit from reviewing how you'll create an income in retirement and whether your current approach remains the right option for your circumstances.

Here are some steps you might consider to protect your pension from the IHT changes.

1. DEPLETE YOUR PENSION DURING YOUR LIFETIME

One of the simplest ways to avoid your pension being subject to IHT is to spend the money during your lifetime.

Working with a financial planner could help you assess what sustainable income you could withdraw from your pension. Creating a cashflow model could help you visualise how your wealth might change over time, depending on your decisions and external factors.

While the outcomes of a cashflow model cannot be guaranteed, it could give you the confidence to spend more in retirement and enjoy this chapter of your life.

You can usually take up to 25% of your defined contribution pension tax-free (up to a maximum of £268,275). When you die, the opportunity to take this tax-free lump sum cannot be passed on to your beneficiaries. So, as part of your retirement plan, you may want to consider when it's appropriate to withdraw this money and how you'll use it.

Please note: The Financial Conduct Authority does not regulate cashflow modelling.

Pension withdrawals may be liable for Income Tax

When you're making pension withdrawals, you might also need to consider your wider tax position.

Pension withdrawals are taxable income. If the withdrawal, combined with any other income you receive, exceeds the Personal Allowance (£12,570 in 2026/27), you will usually be liable for Income Tax.

Additional pension withdrawals could mean you're unwittingly pushed into a higher Income Tax bracket.

2. MAKE GIFTS FROM YOUR PENSION

In addition to spending more money, passing on wealth during your lifetime could be an attractive option.

Gifting might make sense not only from a tax perspective, but also because you could financially support loved ones when they need it most and see the benefits of your gift.

However, it's important to note that not all gifts are considered immediately outside your estate for IHT purposes. See page 11 to find out more about gifting allowances and how gifts are treated when calculating IHT.

You should also consider how taking lump sums from your pension or other assets to make gifts might affect your long-term financial security. A cashflow model could help you understand the implications and allow you to make informed decisions.

3. PURCHASE AN ANNUITY

If you have a defined contribution pension, one option for creating an income is to purchase an annuity, which would provide a regular income for the rest of your life.

The income an annuity provides will depend on rates at the time of purchase and the type of annuity you choose.

Some annuities provide an income that will rise in line with inflation to protect your spending power throughout retirement. You may also choose an annuity that will continue to provide an income for your partner if you pass away first.

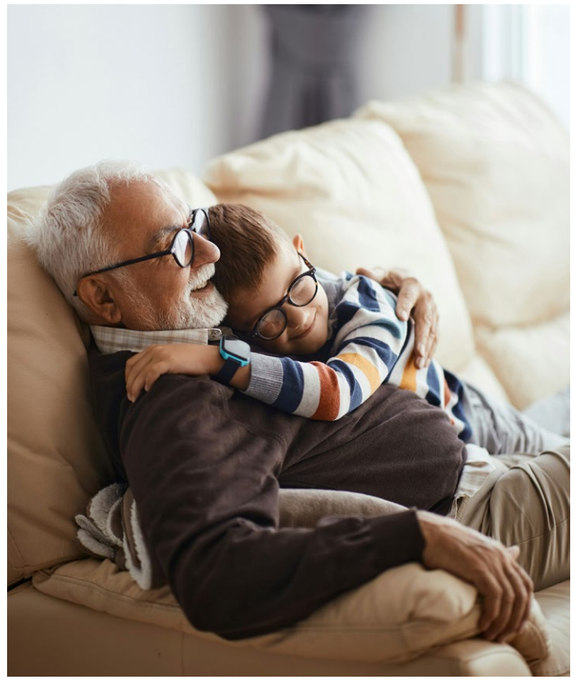
As the money used to purchase an annuity is removed from your pension and estate, it is no longer liable for IHT. However, depending on when you pass away, you may receive less from an annuity than you paid for it, and the difference will not be passed on to your beneficiaries.

As an annuity provides a secure income stream, you might be able to gift the money that remains in your pension under the "regular payments" gifting allowance, which is explained on page 12.

4. CHANGE WHO WILL INHERIT YOUR PENSION

As mentioned previously, you can leave your assets, including your pension, to your spouse or civil partner without them being subject to IHT. As a result, if you currently plan to pass on your pension to another person, changing this could be tax-efficient.

In most cases, your pension is not covered by your will. Instead, you must complete an expression of wish form with each pension provider, setting out who you'd like to receive it.



REVIEWING YOUR ESTATE PLAN COULD HIGHLIGHT OPPORTUNITIES TO IMPROVE TAX EFFICIENCY

When assessing your estate's IHT liability, it could be useful to look at your overall estate plan.

An estate plan considers how you'd like your assets to be managed and distributed, both during your lifetime and after death. It might include writing a will, gifting assets now, and appointing a Lasting Power of Attorney, who could make decisions on your behalf if you lose mental capacity.

How you decide to distribute assets may have a direct effect on your estate's IHT liability. As such, effective estate planning may also involve considering how you could reduce a potential bill.

If you already have an estate plan in place, reviewing it ahead of the IHT reforms could highlight areas where you might benefit from making adjustments. It could mean you're able to pass on more of your wealth to your loved ones now or when you pass away.

GIFTS ARE NOT ALWAYS CONSIDERED OUTSIDE YOUR ESTATE IMMEDIATELY

Many people choose to gift assets during their lifetime to support loved ones. At first glance, it seems like a simple way to reduce or mitigate an IHT bill.

However, some gifts will be considered part of your estate for seven years after they are given for IHT purposes. If you make a gift and then pass away, IHT may be due based on a sliding scale, depending on how long before your death the gift was given. The tax rates on gifts are:

Years between gift and death	Tax to pay on gift
Less than 3 years	40%
3-4 years	32%
4-5 years	24%
5-6 years	16%
6-7 years	8%
More than 7 years	0%

See page 12 for more information about gifting allowances.

Remember that taper relief only applies to gifts in excess of the nil-rate band. It follows that, if no tax is payable on the transfer because it does not exceed the nil-rate band (after cumulation), there can be no relief.

Taper relief does not reduce the value transferred; it reduces the tax payable as a consequence of that transfer.

4 WAYS YOU MIGHT REDUCE A POTENTIAL INHERITANCE TAX BILL

1. CONSIDER INHERITANCE TAX WHEN WRITING YOUR WILL

Your will is legally binding and specifies how you want your estate to be distributed. Your decisions could affect your estate's IHT liability. For example, if you state you want your main home to go to your children, your estate may be able to use the residence nil-rate band.

Similarly, when completing an expression of wish form for your pension, choosing to pass it on to your spouse or civil partner could mean it's not subject to IHT.

2. MAKE USE OF APPROPRIATE GIFTING ALLOWANCES DURING YOUR LIFETIME

Gifting allowances could allow you to pass on assets that will immediately fall outside your estate when calculating the IHT due. Among the gifting allowances you might want to use are:

Annual exemption

Each tax year, you can give up to £3,000 worth of gifts without their value being added to your estate. This is known as your "annual exemption". The annual exemption can be carried forward for one year.

If you want to pass on wealth during your lifetime, using this gifting allowance each year could allow you to gradually transfer assets.

Small gifts

You can give gifts worth up to £250 to as many individuals as you'd like in each tax year, provided they have not received a gift that is covered by your annual exemption.

You may choose to withdraw money from your pension when gifting under these allowances. You should note that pension withdrawals may be subject to Income Tax.

Wedding gifts

Celebrating a marriage or civil partnership provides an opportunity to gift up to £1,000 tax-efficiently.

This allowance rises to £5,000 if your child is getting married and to £2,500 for grandchildren and great-grandchildren.

Regular payments from your income

If you have enough income to maintain your usual standard of living, you can choose to make regular gifts from the surplus income, which would not usually be subject to IHT.

You might use this gifting allowance to:

- Pay your grandchild's school tuition fees
- Cover the care home costs of an elderly relative
- Give monthly support to your child to help with household bills.

For this exemption to apply, the gifts must form part of your normal expenditure, be made regularly, and not affect your ability to maintain your standard of living. You should ensure there's an established pattern of giving and keep good records that demonstrate this to HMRC.

3. LEAVE A CHARITABLE LEGACY

Gifts you make to a charity, either during your lifetime or through a will, are not subject to IHT. A charitable legacy might reduce your tax bill while supporting good causes.

You could use charitable gifts to bring the value of your estate below the IHT thresholds. In addition, if you leave 10% or more of your entire net estate to charity, the IHT rate will fall from 40% to 36%.

You may leave all or a portion of your pension wealth to charity by naming the charity in your expression of wish form.

4. USE A TRUST TO PASS ON ASSETS

A trust is a legal arrangement that could allow you to remove assets from your estate for the benefit of others, while still allowing you to set out how the assets will be used.

In some cases, you could place assets, including pension wealth, in a trust for your beneficiaries so they are outside your estate when IHT is calculated.

Trusts are complex, and there are several different types. Once assets are placed in a trust, it may be difficult or impossible to reverse the decision. In addition, transfers to a trust may be considered part of your estate for up to 14 years.

As a result, it's typically a good idea to seek both financial and legal advice if you're considering using a trust to reduce an IHT bill.

Please note: The Financial Conduct Authority does not regulate will writing or trusts.

Life insurance could pay an Inheritance Tax bill

While life insurance won't reduce your IHT bill, it could provide your loved ones with a way to pay it.

Life insurance would pay out a defined lump sum to your beneficiaries when you pass away, assuming you've made the premium payments. This could reduce stress for your loved ones and help ensure your assets are passed on intact.

It's important that your life insurance policy is written in trust. Otherwise, the payout may be included in your estate and increase the IHT bill.

An estate plan could highlight other ways to improve tax efficiency

Depending on your circumstances, there may be other steps you can take to reduce an IHT bill, or further tax reliefs available to you. Please contact us to discuss how we can help you create a tax-efficient estate plan.

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Get in touch

If you'd like to create a tailored retirement and estate plan that considers your estate's IHT liability, please contact us:

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Please note: This guide is for general information only and does not constitute advice. The information is aimed at individuals only.

All information is correct at the time of writing and is subject to change in the future.

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A pension is a long-term investment not normally accessible until 55 (57 from April 2028). The fund value may fluctuate and can go down, which would have an impact on the level of pension benefits available. Past performance is not a reliable indicator of future performance.

The tax implications of pension withdrawals will be based on your individual circumstances. Thresholds, percentage rates, and tax legislation may change in subsequent Finance Acts.

Remember that taper relief only applies to gifts in excess of the nil-rate band. It follows that, if no tax is payable on the transfer because it does not exceed the nil-rate band (after cumulation), there can be no relief.

Taper relief does not reduce the value transferred; it reduces the tax payable as a consequence of that transfer.

The Financial Conduct Authority does not regulate Inheritance Tax planning, estate planning, cashflow modelling, will writing, trusts, or Lasting Powers of Attorney.

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