

Changes to inheritance tax (IHT) on pensions from 2027

In the Autumn Budget, the Chancellor said that inheritance tax thresholds, which are the amount you can pass on when you die, before inheritance tax is due, are staying the same until 2030. But, from April 2027, pensions will no longer be exempt from inheritance tax. That means that inheritance tax may have to be paid on your pension when you die.

It's important to note that we don't yet have the finalised legislation, so things could change. We are also still waiting on more detail.

How inheritance tax on pensions currently works

Currently, defined contribution pensions, where you build up a pot of money to give you an income when you retire, wouldn't normally be part of your estate and there would be no inheritance tax to pay. The 'estate' simply means all the assets, like a house, investments or valuables, that someone owns when they die. But from 6 April 2027 defined contribution pensions will be subject to inheritance tax. The standard rate of inheritance tax is 40%.

Who will be affected by the change to inheritance tax?

Even with this change, inheritance tax isn't going to be an issue for most people. That's because everyone has an entitlement to a nil rate band of £325,000 of assets which they can leave to anyone free of inheritance tax. This is also known as the inheritance tax threshold.

We know that many people don't have enough in their pension for the lifestyle they'd like in retirement, so they may not have much, if any, money left in their pension(s) when they die. Often pensions are passed onto the pension saver's husband or wife and if they don't have their own pension, or only have a small pension, then they will need that pension to top up any pension savings they have. Government figures estimate that 10,500 estates will pay inheritance tax for the first time, as a result of the changes to the rules on inheritance tax and pensions, and 38,500 will pay more inheritance tax.

But if you own your own home, then when your defined contribution pension is added onto this, it might be more than the amount you're able to pass on free of inheritance tax. And that could mean inheritance tax has to be paid when you die or when your husband or wife dies.

If you are married or have a civil partner

If a couple are married and live in the UK, then when the first member of the couple dies, and anything they own is passed onto their husband, wife or civil partner then there is no inheritance tax to pay. This means that some or all of the £325,000 inheritance tax nil rate band which was unused on the death of the first person can be transferred to the surviving husband, wife or partner. So, this means that up to £650,000 (2 x £325,000) is available when the surviving husband or wife dies, before inheritance tax is paid.

