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Inheritance tax on pensions

Proactive submission by the Chartered Institute of Taxation

1. Executive Summary

- 1.1. The Chartered Institute of Taxation (CIOT) is the leading professional body in the UK for advisers dealing with all aspects of taxation. We are a charity and our primary purpose is to promote education in taxation with a key aim of achieving a more efficient and less complex tax system for all. We draw on the experience of our 20,000 members, and extensive volunteer network, in providing our response.
- 1.2. We recommend six targeted legislative changes to the inheritance tax (IHT) regime for pension interests before the new rules take effect on 6 April 2027.
- 1.3. The provisions introduced by the Finance Act 2026, which bring most unused pension funds and death benefits within the scope of IHT, give rise to several practical and technical issues. Unless these issues are addressed, the new regime could result in unfair outcomes, delays in estate administration and significant additional compliance burdens for personal representatives (PRs), pension scheme administrators (PSAs) and especially HMRC. We highlighted these issues in a letter to the Financial Secretary to the Treasury dated 31 July 2026.
- 1.4. That letter identified five key areas where legislative amendment is needed. This submission adds a further point: the removal of the undue hardship requirement for a company purchase of own shares. We previously recommended this change in the context of the reforms to agricultural and business property relief (APR/BPR) changes, but the relaxation of the rules would also be of benefit to those with business property in pensions.

2. Pension funds discovered after administration has completed

- 2.1. During the early stages of the administration of a deceased estate, assets belonging to the deceased may not always come to light, leading to unexpected IHT liabilities later on. PRs will typically hold back some of the estate to cover this eventuality. Where pensions differ is that the PR has no control over the pension funds. The funds do not remain where they are until they are claimed. Instead, PSAs control the funds and will pay out the pension to the pension beneficiaries even if they have not received any communication from the PRs

(indeed, they are encouraged to do so at the earliest opportunity). This leaves the PRs to pick up the liability, with the hope that they will be refunded by the pension beneficiaries.

- 2.2. In recognition of this unsatisfactory state of affairs, the legislation provides a degree of protection. Where a previously unidentified pension fund is discovered after HMRC has issued a certificate of discharge, the PRs will not be held personally liable for the additional tax due on the pension, provided they took reasonable care. Of course, getting a certificate of discharge is often not quick and many simple estates have not bothered doing so. Given the personal liability imposed on PRs in the absence of such a certificate it is inevitable that far more estates will seek such a certificate, imposing additional burdens on HMRC.
- 2.3. Guidance as to what constitutes reasonable care is needed as soon as possible for professionals to plan. A particular issue is that a newly discovered pension creates additional tax not only on the pension itself but on the other assets in the estate, as well as on certain trusts in which the deceased had an interest. HMRC have suggested that they would collect this extra tax “following existing processes”, though it is not clear whether PRs and trustees, having already wound up their work, would remain responsible for calculating and reporting the extra tax. It is anticipated that they would at least need to give HMRC full details of all residuary beneficiaries from whom to collect the extra IHT.
- 2.4. The additional tax arises on multiple assets (and therefore potentially multiple beneficiaries) because of the way the IHT allowances (the nil rate band and transferable nil rate band) must be pro-rated across the estate and each pension. This mechanism creates a proportionate reduction in allowances each time a new pension is identified. Further, where the estate qualifies for the residence nil rate band and transferable residence nil rate band, the adjustments may be magnified because those allowances are also reduced in proportion to the value of the assets in excess of a fixed threshold.
- 2.5. The interaction of the above mechanisms with the plans to bring pension interests into the estate administration process will cause complexity, and with it added confusion and costs for families of the deceased. HMRC will also face higher costs and resource pressure as it attempts to reassess and collect small amounts of additional tax from multiple beneficiaries and trusts. This will only increase as increasing numbers of estates are brought within the scope of IHT.
- 2.6. A simple fix to this would be to impose the estate rate on any pensions discovered after the certificate of discharge which is simply paid by that pension beneficiary and the PSAs are under an obligation to notify HMRC of such payments (similar to the chargeable event legislation where the insurance companies have to notify HMRC). That avoids having to recalculate the rest of the estate.

3. Loss relief should be available for pension assets

- 3.1. The Finance Act 2026 which brought pensions into the scope of IHT did not introduce an equivalent to the existing IHT loss relief provisions applying to land and quoted shares.
- 3.2. Currently, relief may be available where qualifying assets are sold within a prescribed period after death at a value lower than that returned for IHT purposes. But this will continue to apply only to the estate assets, not the pensions subject to IHT from 6 April 2027.
- 3.3. Many pension arrangements hold investments that can experience substantial fluctuations in value, including quoted shares, collective investment funds and, in some self-invested personal pensions (SIPPs) and small self-administered schemes (SSASs), commercial property. Where IHT is charged by reference to the value at death but the underlying assets subsequently fall in value before being realised, beneficiaries will pay tax on

value that they never receive. There is a risk that, in practice, investment managers feel they have no alternative but to sell at least some of the share portfolio straight after death to avoid the risk of falling values without a commensurate IHT reduction.

- 3.4. The CIOT therefore recommends a dedicated loss relief regime for pension funds, allowing relief where pension assets are actually sold by the PSA within 12 months of death. Such a measure would align the treatment of pension wealth more closely with the treatment of comparable assets held directly in an estate.

4. Instalment payment provisions should be extended

- 4.1. A long-standing feature of the IHT system is the ability to pay tax by annual instalments where the charge arises on certain illiquid assets, including land, business property and shares in unquoted companies. The purpose of these provisions is to help with cash-flow difficulties where tax becomes payable before assets can be sold.
- 4.2. However, the Finance Act 2026 changes do not extend the instalment option to pension assets. As a result, IHT attributable to pension benefits will generally become payable within six months of the end of the month of death, irrespective of the liquidity profile of the underlying investments.
- 4.3. The CIOT believes that if the policy objective is to achieve comparable taxation of pension and non-pension wealth, the instalment regime should be available where assets held within a pension arrangement would meet the ordinary qualifying conditions if owned directly. This would reduce liquidity pressures and help ensure that tax liabilities can be met without forcing inappropriate or premature disposals.

5. The charitable giving reduced rate requires reform to avoid complexity and unfairness

- 5.1. The interaction between the pension IHT reforms and the reduced 36% rate of IHT for estates leaving at least 10% to charity gives rise to significant practical difficulties, extreme complexity and unfairness for those impacted. The reduced rate rules were designed to encourage charitable giving by reducing the rate of tax on the relevant component of an estate from 40% to 36%.
- 5.2. The CIOT notes that bringing pension assets into the "general component" will produce results that were never intended by testators. Fixed charitable legacies may cease to satisfy the 10% threshold once pension wealth is included in the relevant calculations. Conversely, percentage-based charitable legacies may generate larger gifts than intended, reducing the inheritance received by residuary beneficiaries while potentially producing a tax advantage for pension beneficiaries who make no contribution to the charitable donation.
- 5.3. In addition to these unintended outcomes, the calculations are likely to become considerably more complex, creating excessive work for PRs, PSAs and HMRC.
- 5.4. The CIOT therefore recommends that pension assets should form a separate pension component, to be treated separately from the general component for the purposes of the reduced-rate calculation, in a manner consistent with the treatment of all other categories of assets falling outside the free estate – such as with the settled property component. This would preserve the policy objective of encouraging charitable giving while avoiding unnecessary complexity and disputes. In practice, as well as simplifying the process for HMRC, it should not have a significant effect on the tax take. Indeed it may well avoid unplanned larger payments to charities from estates, to meet the higher 10% test if pensions are included in the general component, leading to larger reductions in IHT.

6. The six-month payment deadline is unrealistic and unreasonable

- 6.1. The existing deadline for paying IHT is no longer reasonable given the added administrative complexity of pensions being brought into scope. This is compounded by the APR/BPR changes, which will now require more time-consuming thorough valuations to be carried out for estates holding an interest in a business or farmland.
- 6.2. We note that, once the new pension reporting requirements are taken into account, PRs may have substantially less than six months to establish the estate's IHT liability and arrange payment. This will be a challenging process for simple estates; for complex estates, or any estates where there are a number of separate pensions, high interest charges on late payment will inevitably need to be accounted for as standard. This strikes us as particularly unfair in light of the recent increases to interest charges which are now at a penal level. The rationale for this change was to encourage early payment of a known liability. We cannot imagine that a penal rate of interest was envisaged as a penalty on grieving families with pension details needed from different PSAs, within an unreasonably short timeframe.
- 6.3. We therefore recommend the government reconsider the six-month payment deadline, at least during the initial years of the new regime while pension administrators, taxpayers and HMRC adapt to the changes. Our suggestion would be to align the deadline for paying the IHT with the 12-month deadline for filing the IHT calculations, which is surely justified despite the impact on the Exchequer. Alternatively, there could be at least a 12-month payment deadline for the share of IHT due on the pension funds or a reduction in the rate of interest charged on late payment of IHT in the first year to a more reasonable rate.

7. Funding IHT liabilities in family companies

- 7.1. Restrictions to APR/BPR will obviously increase the number of estates facing IHT liabilities where the wealth is held primarily in family companies rather than in personally held liquid assets.
- 7.2. Funding an IHT liability where the asset on which the tax is due is tied up in the business becomes even more problematic where part of that business is held by a pension scheme. For self-invested pension schemes and small self-administered pension schemes in particular, the inextricable connection between the deceased's taxable wealth and the business may lead ultimately to the company needing to be sold at an undervalue or liquidated.
- 7.3. In such cases, a company purchase of own shares can be the most practical way of providing funds to pay the IHT arising on the death of a shareholder without resorting to expensive loans or high-pressure sales of assets at undervalue. The current rules, however, restrict the use of a company purchase of own shares to only those scenarios where the PRs would face undue hardship without it.
- 7.4. When APR/BPR was unlimited, there was little need for these provisions. That is no longer the case.
- 7.5. We recommend that families are supported to fund these increased liabilities through a minor modification to the existing legislative framework. By removing the undue hardship condition, companies can help fund IHT on their own share capital without PRs having to take arduous steps to prove they have exhausted all other options.

8. Conclusion

- 8.1. The CIOT respects the policy decision to create a coherent framework for the taxation of pension wealth on death. However, we believe that several technical aspects of Finance Act 2026 would benefit from comparatively minor amendments if the regime is to operate fairly and efficiently in practice. The CIOT has invited HM Treasury and HMRC to engage with stakeholders on these issues and has offered to assist in developing workable solutions ahead of the commencement of the new rules in April 2027.

9. Acknowledgement of submission

- 9.1. We would be grateful if you could acknowledge safe receipt of this proactive submission.

The Chartered Institute of Taxation

The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. Our comments and recommendations on tax issues are made solely in order to achieve this aim; we are a non-party-political organisation.

Our stated objectives for the tax system include:

- A legislative process that translates policy intentions into statute accurately and effectively, without unintended consequences.
- Greater simplicity and clarity, so people can understand how much tax they should be paying and why.
- Greater certainty, so businesses and individuals can plan ahead with confidence.
- A fair balance between the powers of tax collectors and the rights of taxpayers (both represented and unrepresented).
- Responsive and competent tax administration, with a minimum of bureaucracy.

The CIOT's work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.

The CIOT draws on our members' experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries.

Our members have the practising title of 'Chartered Tax Adviser' and the designatory letters 'CTA', to represent the leading tax qualification.