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Rt Hon James Murray MP
Financial Secretary to the Treasury
HM Treasury
By email - Action.FST@HMTreasury.gov.uk

Dear Minister,

Inheritance tax on pensions

Our letter of 24 July highlighted the Finance Act 2026 changes to bring pensions within scope of inheritance tax (IHT) from 6 April 2027 as a priority issue on which we would write separately. We believe some important aspects need urgently addressing to better deliver the policy and make it workable in practice. Without further legislative change, the new charge will produce unfairness, dispute and delay between personal representatives (PRs), pension scheme administrators (PSAs) and beneficiaries, and considerable additional compliance work for HMRC.

We recommend legislating for five key changes:

1. Pension funds discovered after the certificate of discharge

A pension fund discovered after a certificate of discharge is issued would apparently require HMRC to recalculate the residence nil rate band, reapportion the nil rate band (NRB) and collect further tax from every beneficiary – including any continuing Will trust. This is a highly unsatisfactory result creating considerable cost to HMRC and uncertainty for families and trustees.

We suggest legislation providing that any pension discovered after the certificate of discharge is simply taxed at the estate rate without the benefit of any NRB otherwise available on death, save to the extent it was not fully used.

2. Loss relief

FA 2026 contains no pension equivalent for the loss relief on land/quoted shares that is available in free estates. This is despite pensions commonly holding (and indeed encouraged to hold by government) volatile quoted investments (and, in SIPPs and SSASs, commercial property).

This creates an inequitable outcome: IHT may be charged on values that beneficiaries never receive. The issue is particularly acute where funds must be crystallised or transferred within specific timeframes, potentially forcing sales at unfavourable times.

We suggest each pension fund be treated separately for loss relief purposes provided there is an actual sale by the PSA within 12 months of death.

3. Payment by instalments

The long-established option to pay IHT by instalments exists precisely because IHT on illiquid assets creates cash-flow problems. FA 2026 does not extend the instalment rules to pensions, leaving the full liability due within six months of death. If the policy intention is fairness between pension wealth and other forms of wealth, the instalment option should apply where assets within pensions meet the same conditions as assets outside them.

4. The reduced 36% IHT rate where 10% of the estate is left to charity

The effect of FA 2026 is that the reduced rate calculation will no longer work as expected. Gifts will often fail, giving rise to confusion and disputes, and a sense of injustice since the policy is designed to encourage charitable giving.

As an example, a fixed £100,000 legacy against a £1m free estate fails once pensions increase total assets (“the general component”) over £1m. Alternatively, a percentage legacy of 10% of the general component will produce a larger charitable gift than the testator intended, at the expense of the residuary beneficiaries and the Exchequer, while the pension beneficiary benefits from the 36% rate without contributing to the legacy.

If the general component covers all pensions as well as the free estate, it will make it more complicated and impractical in many cases to claim.

We recommend legislating to separate pension assets from the general component, in the same way as other taxable assets outside the free estate. We believe this would be a simple legislative fix.

5. The six-month payment deadline

The six-month deadline is unrealistic in the context of FA 2026 changes. In practice, the 35-day notification period leaves PRs less than 5 months to obtain information from multiple schemes, obtain valuations and establish exemptions and reliefs. Neither HMRC nor PRs will want the cost of paying IHT upfront and reclaiming it once spouse exemption is confirmed.

PRs will hesitate to distribute the free estate until all pension IHT liabilities are discharged. PSAs are also reluctant to act on PRs’ instructions before probate, meaning interest on IHT will accrue almost automatically – an unfair outcome for beneficiaries, PRs and PSAs alike.

We strongly urge reconsideration of the deadline, even temporarily while new PSA processes are ironed out.

We would welcome the opportunity to meet to discuss these issues in more detail. We would also be pleased to work with officials on how we think these remedies could be legislated/implemented. In line with our normal practice, we intend to publish this letter, and any response, on our website (tax.org.uk).

Yours sincerely

EMilner

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