

## **A British Expat's Guide to U.K. Pensions & Inheritance Tax (IHT) Changes**

### **Summary**

- Under recent draft U.K. legislation, from 6 April 2027, most unused U.K. pension funds and pension death benefits will be counted inside your estate for U.K. IHT—a major shift from today's "IHT-free" treatment.
- U.K. connected spouses/civil-partners and charity exemptions remain; death-in-service benefits are excluded.
- IHT thresholds are frozen through 5 April 2030: Nil-Rate Band (NRB) allowance £325,000; Residence Nil-Rate Band £175,000 (subject to a taper above £2M estates).
- Your personal estate representatives (Executors), not the pension administrator, will be responsible for reporting and paying any IHT due on U.K. Pensions.
- For U.S. resident expats, U.S./U.K. Treaty rules still govern income taxation of pension withdrawals, but the new IHT rules are separate and apply at death. U.K. IHT will carry a U.S. credit for Estate Tax purposes.

### **U.K. Pension Types**

#### **Defined Contribution (DC)**

- **Personal, Occupational, Workplace & Stakeholder Plans**  
Employer/employee contributions invested in funds. Flexible access from age 55 (rising to 57 from April 2028). Death benefits: cash lump sums and/or nominee drawdown. Under the 2027 rules, unused funds/lump sums fall into the IHT estate; spouse/charity exemptions apply.
- **Self-Invested Personal Pension (SIPP)**  
Wider investment choice (including U.K./overseas securities, cash, sometimes commercial property). Property or cash left in a SIPP forms part of the estate for IHT from 6 April 2027 (executor pays).

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- **Small Self-Administered Scheme (SSAS)**

Company-sponsored DC plan for directors, now less popular given expense versus SIPPs; can hold employer premises/loans. Unused funds and death-benefit lump sums will be within the estate from 2027.

**Defined Benefit (DB / Final Salary)**

- Promises an income for life based on salary/service; may pay dependent's (spouse) pensions. From 2027, most DB lump-sum death benefits; what's out: dependents' scheme pensions (ongoing survivor income) and charity lump-sum death benefits.

**Note:** The Lifetime Allowance was abolished on 6 April 2024 and replaced with the Lump Sum Allowance (LSA £268,275) and Lump Sum & Death Benefit Allowance (LSDBA £1,073,100) which cap tax-free lump sums; income tax may apply beyond these allowances. These interact with, but are separate from, the new IHT rules.

**U.S. Tax & Reporting for U.K. Pensions (U.S. residents)**

- **Income taxation:** Under the U.S.–U.K. treaty, pensions are generally taxable only in the country of residence (the U.S.) when paid; and amounts that would be exempt in the U.K. (e.g., the 25% Pension Commencement Lump Sum or PCLS) should be considered in the context of a Treaty Position (via Form 8833). It's important to seek advice from a cross-border accountant who can advise, potentially submit a tax return with substantial authority and qualify for safe harbor in the event of an IRS challenge.
- **Reporting:** Many U.K. pensions are specified foreign financial assets or trusts and may be reportable on Forms 8938, or 3520 and sometimes on FBAR (FinCEN 114) if thresholds apply. These are separate from income tax and still required even when no U.S. tax is due.
- **Transfers:** There are no HMRC-listed QROPS (offshore pensions) eligible in the United States, so you can't roll a U.K. pension into a 401(k)/IRA without punitive "unauthorized payment" charges; overseas transfers to QROPS can also trigger a 25% Overseas Transfer Charge unless strict conditions are met.

**DB vs DC IHT Impact**

**Those most affected:** Large DC/SIPP/SSAS balances intended for heirs; lump-sum-heavy DB schemes.

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**Those exempted:** DB pensions paying dependents' income; death-in-service; charity-directed benefits.

### **2027 IHT Illustrative impact**

**Before 2027:** SIPP £600k ignored for IHT.

**From April 2027:** SIPP £600k now included for IHT, so £325k NRB applies, so net IHT liability of £110,000 payable, assuming no eligible U.K. spouse/civil partner.

### **Planning strategies for British expats with >£325,000 in U.K. pensions**

Your optimal mix depends on your family situation, ages, health, and cash-flow need.

The planning points below are the levers we typically evaluate and model as part of our ongoing advice for clients in retirement:

#### **1. Re-order your decumulation/income sequencing**

Consider spending pensions earlier (within your LSA/LSDBA and bracket-management for U.S. tax) while retaining/growing non-pension assets earmarked for beneficiaries. This can shrink the IHT-exposed pension base (but stay aware of U.S. tax brackets, NIIT, and state tax.)

#### **2. Use the spouse exemption deliberately**

If your spouse/civil partner is eligible, designate them as first beneficiary to keep 0% IHT on first death. On the survivor's death, remaining pension funds would be in scope, so plan second-death exposure using gifts, spending, or insurance. Where the surviving spouse is not a U.K. or U.S. citizen, coordinate QDOT (U.S. marital deduction) and U.K. spouse rules.

#### **3. Consider partial Annuitization**

Converting a proportion of your DC scheme to a lifetime annuity can trade flexibility for IHT efficiency, since dependents' scheme pensions (ongoing income) are outside IHT scope; many joint-life annuities are also carved out in HMRC's proposals. This can be powerful for those with longevity in the family.

#### **4. Charitable legacies**

Naming a registered charity for a portion of lump-sum death benefits preserves an

IHT exemption for that slice and can reduce the blended effective rate on the rest of the estate.

**5. Lifetime (7-years) or Surplus Income Gifting**

Drawing from pensions (tax-managed in the U.S.) and gifting earlier can remove assets from the U.K. estate if you survive seven years. Additionally, regular gifts from excess income are immediately IHT-exempt if they do not impact your standard of living. It is advisable to coordinate with U.S. gift/estate exemptions and annual exclusions, and document gifts carefully.

**6. Whole-of-Life (Whole Life) Insurance in Trust**

Use U.S. or U.K. Whole-of-Life/Whole Life to liquidity-match the projected IHT bill on pensions; hold policies in an appropriate trust to keep proceeds outside the estate (and avoid probate delays).

**7. Keep death-in-service benefits**

For employed expats with U.K. schemes, death-in-service remains outside IHT—do not inadvertently replace it with IHT-exposed structures whilst eligible, unless there's compensating benefit.

**8. Update nominations & letters of wishes**

Make sure provider nominations reflect your new plan (spouse first, charity portion, etc.). With executors now liable to pay/report IHT on pension wealth, ensure your Will coordinates who ultimately bears the tax (estate vs. pension beneficiaries) to avoid family disputes.

**9. Avoid costly “tax escape” strategies**

- No transfers to a U.S. 401(k)/IRA: there are no U.S. QROPS, and non-QROPS transfers are treated as unauthorized payments (punitive U.K. charges).
- Moving to an overseas pension/QROPS is often OTC-exposed (25%) and, per draft rules, overseas pension death benefits can be looked-through for IHT anyway—so “offshoring” is rarely a fix for U.K. IHT.

**10. Model the age-75 crossover & LSDBA**

Beneficiary income tax outcomes differ depending on whether death is before/after 75 and whether LSDBA has been used; pair this with the new IHT layer to sequence withdrawals sensibly.

### **Practical Checklist for U.S.-resident British Expats**

1. **Inventory:** Identify your U.K. pensions (provider, type, current value, nominations, death-benefit options).
2. **Will & Executors:** Update U.K./U.S. Wills, add instructions on pension IHT and which pool bears the tax.
3. **Beneficiary design:** Spouse first? Charity portion? Partially Annuitize?
4. **Cash-flow & tax map:** Create a U.S.-centric withdrawal plan, while aiming to reduce IHT-exposed balances.
5. **Insurance gap analysis:** Consider level or whole-of-life held in trust policies to fund projected IHT on pensions.
6. **Reporting:** Confirm FBAR/8938/3520 coverage of foreign pensions where required.

### **Frequently asked questions**

#### **Can I move my U.K. pension into a U.S. 401(k) or IRA?**

No. The U.S. has no HMRC-listed QROPS, and non-QROPS transfers are treated as unauthorized payments (very high U.K. charges).

#### **Is the U.K. 25% tax-free lump sum (PCLS) taxable in the U.S.?**

Depending on your circumstances, a Treaty Position can be considered but you should seek personal advice from a U.K./U.S. cross-border Accountant who is able to submit an opinion with Substantial Authority.

#### **Will a DB survivor's pension hit IHT from 2027?**

Generally no—dependents' scheme pensions remain outside IHT scope; lump-sum DB death benefits are typically in scope.

#### **How can Fawley Wealth International help?**

- Coordinated U.S.–U.K. tax modeling of withdrawals, LSDBA planning, and second-death IHT projections.
- Trust & Estate planning: Wills/beneficiary design, insurance in trust, charitable structuring, referring to our Cross Border Solicitors/Attorneys when relevant.
- Coordinate with a specialist cross-border Accountant: 8833 treaty claims, FBAR/8938/3520 awareness, and cross-border Executor planning.

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