Pensions tax relief administration: call for evidence

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The Low Incomes Tax Reform Group welcomes publication of a call for evidence on the administration of pensions tax relief, hoping that it will result in redressing the balance for low income workers who currently do not get tax relief on pension contributions where their employer chooses a pension scheme operated on a net pay basis.

Tax relief on individual pension contributions can be given in two ways:

1. Relief at source (RAS): with a contribution net of basic rate tax being made by the individual and the pension scheme claiming a basic rate top-up direct from HMRC; or
2. Net pay arrangement (NPA): where the employer deducts the employee's pension contribution from gross pay before income tax.

Those earning around or below the personal allowance who contribute to an employer's NPA scheme will pay 25% more for their pension contribution than an equivalent employee in a RAS scheme. This is because the NPA contributor gets no tax relief as a result of their contribution being deducted from gross pay, whereas the RAS contributor pays the net amount and the tax relief reclaimed by the scheme is not clawed back – despite them not being a taxpayer.

So for non-taxpayers, £100 of pension savings would cost:

- £80 under RAS; and
- £100 under NPA.

LITRG have been working with various other individuals and bodies across the pensions industry to look at ways in which this imbalance could be redressed. The combined efforts of this 'net pay action group' succeeded in securing a 2019

Conservative Party manifesto commitment to review the issue. Delivering on this promise, HM Treasury published a call for evidence on 21 July 2020 (https://tinyurl.com/y55frnw5).

As explained in our 2020 Budget submission ('LITRG Budget representations', March 2020), our proposed solution is for HMRC to identify those who have 'missed out' on tax relief due to being enrolled in an employer's NPA scheme. They could then provide an equivalent savings incentive – a kind of 'notional tax relief' to level things up. While our proposed solution is included as a suggested approach in the call for evidence, it is disappointing to note that the initial view is that government is not minded to proceed with it.

Other proposals are:

- **To raise a standalone tax charge in respect of RAS contributors who are not strictly entitled to 'tax relief' because they are non-taxpayers**
  This would amount to a levelling down and the call for evidence notes that the government is also not minded to proceed with it.

- **Employers to operate multiple schemes**
  Essentially, this means employers would put non-taxpaying employees into RAS schemes and other employees into NPA schemes. While this might be an option for larger employers who could potentially absorb the administrative burden, it would not be practicable for smaller employers. Similarly, it poses problems where the employee has another source of income, such as working elsewhere for a different employer. Someone could appear to the employer to be a non-taxpayer based on a single source of employment income, but could be a taxpayer when combining it with other sources.

- **Mandating the use of RAS for all defined contribution schemes**
  This might result in tax relief being given to many of those who are currently missing out under NPA, but not all, given that it would not include defined benefit schemes. In addition, it would mean that those entitled to tax relief above the basic rate would have to claim it back from HMRC, whereas relief at the correct rate is given automatically under NPA.

LITRG look forward to working with HM Treasury in responding to the call for evidence, continuing to make the case for HMRC to make a balancing payment to

affected individuals.

The full response will be available after the response deadline of 13 October at: www.litrg.org.uk/latest-news/submissions.