Pension tax relief errors: LITRG's new report

Employment Tax | General Features | Management of taxes

22 June 2026

LITRG have released a short position paper entitled 'Workplace pensions – a hidden problem'. Here, we share a summary for practitioners.

An under-recognised payroll and pension administration issue may be giving some employees double pension tax relief, while storing up PAYE problems for employers. Tax practitioners may have seen such errors or may already be helping employers to regularise their positions. Our new position paper makes recommendations aimed at preventing such problems from arising in the first place and making them easier to resolve when they do, hopefully saving considerable effort for all concerned.

The paper begins by describing the issue in detail. It arises where pension contributions to a relief at source (RAS) scheme are processed through payroll as if the scheme were a net pay arrangement. In that case, tax relief is given once through PAYE because taxable pay is reduced, and again when the pension provider claims basic-rate relief from HMRC. The result is incorrect PAYE, inaccurate real time information (RTI) data and potential employer exposure to arrears, interest and penalties.

The paper sets out how the problem is probably being driven by confusing payroll terminology, poor employer understanding and awareness, and difficult correction processes. HMRC's RTI wording of 'contributions paid but not under net pay arrangements' is far from user-friendly. For small and micro employers, including individual employers, and especially those using HMRC's Basic PAYE Tools, it is easy to see how pension contributions could be keyed into the wrong field and left that way for months or years.

There are compliance implications for employers. Where RAS contributions have been wrongly treated as net pay arrangement, the primary error lies in the operation of PAYE. Depending on the timing and scale, the employer may need to make a voluntary disclosure. However, the paper highlights that the disclosure process is outdated and that correcting the position may be complicated by the need to unwind excess pension contributions.

For example, payroll may be configured so that the employer deducts and remits 100% of the intended gross contribution to the pension provider, rather than the 80% employee contribution that should have been paid under RAS. Where pension providers are unwilling or unable to refund or adjust those excess contributions promptly, employers may face additional administrative burdens and costs. Furthermore, making a disclosure may not correct the underlying RTI data that incorrectly records the type of pension arrangement.

This matters because HMRC is preparing to roll out the FA 2004 s 193A top-up regime for low earners in net pay arrangements – something LITRG, as part of the Net Pay Action Group, has long called for. Those payments will depend on HMRC using RTI data to identify who is in a net pay arrangement. If that data is wrong, some workers could miss out on payments they should receive, while others could be paid in error. In other words, pension tax relief misclassification could start to distort delivery of an important low-pay policy reform.

The paper accepts that recent evidence on the scale of the problem is limited. However, the available indicators, including practitioners writing helpfully to LITRG in response to our earlier articles on the issue (thank you!), all suggest it could be significant.

The paper makes a series of practical recommendations. These include:

- changing HMRC’s RTI terminology to use clearer RAS wording;
- improving employer guidance and communications;
- modernising disclosure processes;
- ensuring that corrections also address or flag RTI pension data;
- clarifying expectations of pension providers where excess contributions must be unwound; and
- using HMRC’s own data to estimate the scale of the problem.

Overall, the paper is a call for HMRC, The Pensions Regulator and pension providers to work together and treat pension tax relief misclassification as a real and serious issue that needs resolving.

For payroll professionals and tax advisers, the paper is a reminder to sense-check pension tax relief handling whenever they take on new payroll work, review auto-enrolment compliance or deal with historic PAYE irregularities. What looks like a small payroll setup error may in fact be a long-running tax and pensions compliance problem, with wider implications than many clients will realise.

LITRG’s full paper is available here:
[Workplace pensions - hidden problem]

Meri McCammond *mmccammond@litrg.org.uk*