HM Treasury Call for Evidence – Pensions Tax Relief Administration
Response from the Low Incomes Tax Reform Group (LITRG)

1   Executive Summary

1.1   For some time, we have been looking at how all low-income earners could be given tax relief on their pension contributions – irrespective of the scheme chosen by their employer (which dictates the method of tax relief used).

1.2   In summary, together with other members of the Net Pay Action Group (see below), our response to this call for evidence is as follows:

- Action <u>must</u> be taken to ensure all low-income workers get a government contribution to their pension, as was promised under auto-enrolment. The gap between those in Net Pay Arrangements (NPA) and Relief At Source (RAS) schemes will only grow as auto-enrolment is extended to 18-year-olds and the lower earnings limit is removed.

- Failure to take action could damage confidence in pensions and auto-enrolment.

- The social injustice in the current situation – with nearly three-quarters of those affected being women – must be rectified.

1.3   We continue to press for HM Revenue & Customs (HMRC) to deliver the solution put forward in our previous submissions[1] ('suggested approach 1' in the call for evidence). We

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[1] See our 2020 Budget representation: https://www.litrg.org.uk/latest-news/submissions/200204-budget-representation-2020-net-pay-action-group

believe the call for evidence misrepresents the impacts of this approach for the reasons summarised below:

- HMRC already have data from employers via Real-Time Information on contributions made to NPA pensions. There is therefore no need to require schemes to report the same data – hence, there is no additional burden on scheme administrators.

- Similarly, there is no additional burden on employers.

- Payment of equivalent tax relief to NPA scheme members would complicate the income tax calculation. However, the concept behind the refunds could be explained in simple terms and, provided HMRC set out clearly what data has been used in the calculation to arrive at the refund, individuals should be able to check it.

- RAS schemes give tax relief to non-taxpayers. HM Treasury have insisted this is simply because RAS is an administrative easement. This defies logic, as the legislation specifically permits tax relief to not only those who do not earn enough to pay tax (including all self-employed low earners, who can only contribute under RAS), but also to those who do not earn anything at all. We have not received a clear explanation as to why it is not possible to give the equivalent benefit to those in NPA schemes via a different administrative process.

1.4   While we recognise that this solution adds some complexity, it is important to balance the oftentimes competing objectives for the tax system. In this case, we believe that some complexity is a reasonable price to pay to fix the inequality.

1.5   We believe that HMRC making better use of data they already hold is the key to solving this – and other – problems with pensions tax relief. Indeed, HMRC have it in their sights to match data to individuals' records (for example, pre-populating returns). Our recommendation is that HMRC focus early effort on doing this with pension contributions data so that not only can they balance up where low-income NPA contributors have lost out compared to those in RAS schemes, but also they can get the correct rate of relief to RAS members who pay tax above the basic rate.

2   About Us

2.1   *The Low Incomes Tax Reform Group (LITRG)*

2.1.1   LITRG is an initiative of the Chartered Institute of Taxation (CIOT) to give a voice to the unrepresented. Since 1998, LITRG has been working to improve the policy and processes of the tax, tax credits and associated welfare systems for the benefit of those on low incomes. Everything we do is aimed at improving the tax and benefits experience of low-income workers, pensioners, migrants, students, disabled people and carers.

2.1.2   LITRG works extensively with HM Revenue & Customs (HMRC) and other government departments, commenting on proposals and putting forward our own ideas for improving the system. Too often the tax and related welfare laws and administrative systems are not designed with the low-income user in mind and this often makes life difficult for those we try to help.

2.1.3   The CIOT is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT's primary purpose is to promote education and study of the administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.

2.2   *The Net Pay Action Group*

2.2.1   On the subject of equalisation of pensions tax relief for all low earners, LITRG has been working together with Baroness Ros Altmann and a coalition of organisations from across the pensions industry. This 'Net Pay Action Group' (NPAG) consists of pension providers, lawyers, tax specialists, payroll specialists, employers, consumer groups and policy experts.

2.2.2   NPAG has submitted a joint summary response to this call for evidence, with some of its individual members also submitting their own, detailed responses.

3   General comments

3.1   It is in everyone's interests that people save as much as they can into a pension. The issue of low-earners contributing to NPA pensions not getting tax relief on their contribution in the same way as RAS contributors does not *prima facie* affect pension saving levels. The NPA contributor earning beneath the personal allowance puts £100 into their pension, whereas the RAS contributor puts in £80 and this is topped up to £100. Both therefore have £100 in their pension pot.

3.2   The difference is that the NPA contributor has £20 less in their pocket than the RAS contributor in analogous circumstances.

3.3   This might not seem to be a large sum, but to a low-income household even small amounts might be substantial when viewed in proportion to their household circumstances. If, as we understand is planned,[2] auto-enrolment is extended to 18-year-olds and the lower earnings limit is reduced and then abolished such that contributions start from the first £1 of income, the problem will only grow.

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[2] Automatic Enrolment Review 2017: Maintaining the Momentum (see, inter alia, pp 17): https://www.gov.uk/government/publications/automatic-enrolment-review-2017-maintaining-the-momentum

3.4   Based upon auto-enrolment minimum contributions, the maximum 'loss' in 2020/21 (i.e. paying an extra 25% to achieve the same result) for someone earning £12,500 is calculated as follows:

Scheme type	Cost of employee contribution £
NPA (12,500-6,240) x 5%	313
RAS (12,500-6,240) x 4%	250
Difference – i.e. the NPA contributor's 'loss'	**£63**

3.5   Of course, not all low-income earners will be incurring this maximum additional cost. But even if we assume a crude 'average' loss of 50% of this amount, those affected could be losing out something approaching £50 million a year in total – assuming, per para 3.9 of the call for evidence, there are some 1.5 million people affected.

3.6   This difference in cost – hitting those on the lowest incomes – is a social injustice which is at risk of undermining confidence in pension saving, perhaps more so now that household incomes are likely to come under significant pressure due to the economic fallout from coronavirus. An extra £63 could cover the cost of a week's food shopping for the average family, for example.[3] This issue also seems to work against the aim of auto-enrolment 'to support the millions of people not saving enough for retirement'[4], given that those on the lowest incomes are missing out on the tax relief element of that support through no fault of their own.

4   Pension schemes' choice of tax relief

4.1   *Question 1. What are the factors that influence a pension scheme in its choice between using net pay or RAS for their members?*

4.2   Auto-enrolment brought new obligations, phased in by employer size, to provide employees and workers with a workplace pension scheme and, subject to certain criteria, to

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[3] See Money Advice Service, quoting a cost of £60.60 for an average family weekly food shop: https://www.moneyadviceservice.org.uk/blog/how-does-your-household-food-spend-compare

[4] See: https://www.gov.uk/government/publications/automatic-enrolment-evaluation-report-2019/automatic-enrolment-evaluation-report-2019

automatically enrol individuals into the scheme. Minimum contributions are required. With such large numbers of employees joining pension schemes as a result, we understand that many schemes were established using NPA as this method of tax relief is easier (and therefore less costly) to administer. RAS requires additional processes – with schemes having to claim the basic rate relief on contributions, which are obviously not required for NPA where the scheme receives the gross amount from the employer.

4.3   While it is not for us to discuss in detail influencing factors for pension schemes or employers, we think it is important to note that this question is somewhat arbitrary, given that schemes are established and employers will have made their choice of scheme when they reached their auto-enrolment staging date. We therefore are where we are – employers having chosen a scheme which operates on either a NPA or RAS basis (and schemes established accordingly) – and it would seem unlikely that many employers are going to change arrangements voluntarily. We understand that there would be significant costs to schemes to move from NPA to RAS – other members of the NPAG will no doubt be commenting on these in more detail in their own responses to this call for evidence.

4.4   Picking up on para 2.5 of the call for evidence, it is also important to note that as auto-enrolment was phased in, The Pensions Regulator did **not** provide any guidance to employers on the impact on their workers of their scheme's method of operating tax relief. While such guidance is *now* available on their website,[5] and might therefore be borne in mind by new employers and any employers considering a change of scheme, existing employers at the time of auto-enrolment staging would likely have chosen their scheme entirely blind to the issue of low-income workers missing out on tax relief.

4.5   ***Question 2. How do pensions providers currently engage with employers around the differences between net pay and RAS for their employees? Is the method of tax relief a scheme operates a relevant factor in the employer's decision (either directly, e.g. when considering employees' financial positions, or indirectly, e.g. through an impact on provider fees)?***

4.6   No comment.

5   **Suggested approach 1 – paying a bonus using RTI data**

5.1   ***Question 3. Are there ways that this approach could be delivered that would not engage the issues identified, namely the challenges in ensuring consistency across all taxpayers for***

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[5] For example, see: https://www.thepensionsregulator.gov.uk/en/business-advisers/automatic-enrolment-guide-for-business-advisers/6-choosing-a-pension-scheme/what-to-consider-when-choosing-a-scheme#d9567402515148d9a1e35201574bc728 and as noted at para 2.5 of the call for evidence

all aspects of the tax system in a timely fashion, and additional burdens for scheme members and administrators?

5.1.1   The answer to this question lies in clarifying that many of the perceived problems with this solution are either erroneous or over-stated. We therefore approach this answer initially by reflecting on the issues outlined in the call for evidence paper. We pull out below, in italics, parts of the call for evidence paper and then comment on each.

Paras 5.12 and 5.13 – amount of repayment

5.1.2   First, it is necessary to clarify who would be in scope of a repayment. It is not just those having total income below the personal allowance who miss out on tax relief under NPA. Those earning slightly above the personal allowance may also only get partial relief. Scottish income taxpayers at the starting rate of 19% also get only 19% relief under NPA whereas those in RAS schemes get 20%.[6]

5.1.3   Let's say Mr J (resident in England) earns £12,750 in his employment with Y Ltd, which operates a NPA pension scheme. Mr J makes a personal contribution of £350. The personal allowance is £12,500. So Mr J will get tax relief via the payroll on £250 of his contribution, but will miss out on tax relief on the remaining £100 – as compared to someone in his situation contributing to a RAS scheme, who would receive tax relief on the full contribution (by paying £280 net to get £350 gross in his pension) inclusive of £20 relief on that £100.

5.1.4   To resolve this, it would not be necessary to pay out Mr J a basic rate refund on his full £350 contribution and then somehow claw back the excess – perhaps via some adjustment of his personal allowance in his PAYE code. (If you want a three-foot hole, you do not dig a six-foot hole and back-fill three feet of it.)

5.1.5   Instead, the calculation could be adjusted to identify only the **unrelieved** amount and pay out what we might term an 'equalisation payment' to the individual. In this respect, the term 'bonus' used in the call for evidence paper is misleading and inappropriate, as the payment is in the nature of rectifying an inequality, not providing an extra payment to NPA contributors (which might then be misinterpreted as giving them an advantage over RAS members).

'Net pay scheme administrators would have to report their membership to HMRC so that potential bonus recipients can be identified' (para 5.15, bullet 1), and 'It creates disproportionate burdens on… pension scheme administrators' (para 5.20)

5.1.6   Unlike RAS schemes (which are a combination of employment, self-employment and stakeholder pensions and where HMRC have a commercial relationship under which they pay basic rate tax relief over to pension scheme administrators), NPA schemes are exclusively linked to employment relationships and HMRC have no such equivalent

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[6] Though of course Scottish intermediate rate taxpayers get the benefit of 21% relief via NPA.

commercial relationship. Employers give HMRC details of NPA pension contributions via PAYE real-time information (RTI).[7] There is therefore no need for HMRC to collect the same data from schemes. Hence, there would be no extra burden on scheme administrators. This approach simply asks that HMRC match data already in their possession – something which we understand they intend to do under plans to reform tax administration more generally.[8]

5.1.7   To illustrate this point, we have compiled a table below of what information HMRC receive via RAS and what HMRC receive via RTI for NPA members (in the context of determining what tax relief should have been available to them had they contributed via RAS).

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Table: Pension contribution data – RAS v NPA

Data item received from RAS annual returns[Note 1]	Source of the same data item for NPA pension contributors
Member's full name • Title • Forename(s) or initials, if full forenames not known • Surname	RTI data items [Note 2], item 5A RTI data items [Note 2], items 7 and 9 (initials if full forename not known, item 8) RTI data items [Note 2], item 6
Member's full address, including postcode	RTI data items [Note 2], items 13 to 18
Member's National Insurance number (unless the individual does not have one, eg if < 16)	RTI data items [Note 2], item 5
Member's date of birth	RTI data items [Note 2], item 10
Member's gender (if specified)	RTI data items [Note 2], item 11
Member's employment status (employed, pensioner, self-employed, child < 16, other)	RTI submission: It is a 'given' that the individual is an employee as PAYE is being operated and RTI filed.
Rate of relief (based on residency – Scottish, Welsh, rUK)	HMRC determines residence of taxpayers for PAYE purposes and issues the individual code with a prefix 'S' for Scotland [Note 3] and 'C' for Wales [Note 4]

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[7] As acknowledged in the call for evidence, para 2.10.

[8] HMRC, HM Treasury Corporate Report: 'Building a trusted, modern tax administration system', 21 July 2020

	(no such prefix exists for rUK). This is then used by the employer in the PAYE calculation – see RTI data items [Note 2], item 55, 55A and 56

Contribution by:
 	
• The individual
  (also reported by employers, where contributions are made via the payroll - RTI data items [Note 2], item 65)
  or
• third party
	RTI data items [Note 2], item 61
	
	Third party contributions to NPA schemes are not relevant – NPA is an employer/pension provider arrangement. [Note 5]

Life assurance premium contribution	Not applicable to NPA schemes – we understand this relates to old-style pensions term assurance plans which used RAS.
Total amount of transfer payment received	Not applicable – and not relevant to the amount of tax relief due in any case. [Note 6]
Value of member's fund	Not applicable – and not relevant to the amount of tax relief due in any case. [Note 6]
Date of fund valuation	Not applicable – and not relevant to the amount of tax relief due in any case. [Note 6]
Member declaration that their contribution qualifies for tax relief (total contributions are within either 100% of relevant UK earnings or £3,600)	HMRC gathers details of an individual's employment income via PAYE so, when reconciled, the system will 'see' whether contributions are ≤ relevant earnings.

Table notes

[1] https://www.gov.uk/government/publications/how-to-complete-your-annual-return-of-information-for-pension-schemes-operating-relief-at-source-2019-version/how-to-complete-your-annual-return-of-information-for-pension-schemes-operating-relief-at-source-2019-version from 'Annual return of information', reg 15A SI 2005/3448, as inserted by reg 4, SI 2018/150 (https://www.legislation.gov.uk/uksi/2018/150/contents/made)

[2] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/915807/RTI_Data_Item_Guide_21-22_v1-0.pdf

[3] https://www.gov.uk/hmrc-internal-manuals/paye-manual/paye100035#coding

[4] https://www.gov.uk/hmrc-internal-manuals/paye-manual/paye100040#coding

[5] A claim for excess relief may be made if individual contributions exceed the individual's employment income with the employer, or if it is not possible for the employer to deduct the whole amount from the individual's employment income [FA 2004, s 193(4)]. The individual must claim this relief and relief is given by deducting the contribution at 'step 2' of the income calculation [FA 2004, s 193(6)]. This is unlikely to be relevant for those earning around or beneath the personal allowance.

[6] The fund valuation has no bearing on the tax relief due to the individual, except to the extent that for defined benefit schemes, a capitalised increase in value in the 'fund' is relevant for the purposes of determining whether the annual allowance has been exceeded. However, tax relief on the contribution remains due, and a separate annual allowance charge arises in respect of any excess. The individual has a duty under S7 TMA 1970 to notify HMRC of any such liability to tax for the year. This is in any event unlikely to be relevant for those earning around or beneath the personal allowance.

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5.1.8   The above illustrates that HMRC have, via RTI, all the data necessary to reconcile to individuals' records at the end of the year and determine if relief would have been due had NPA contributions been made under RAS – without pension scheme administrators (or employers, as alluded to at para 5.15) incurring any additional burden.

'Members of net pay schemes would have to have their personal allowance reduced' (para 5.15, bullet 2; and para 5.18)

5.1.9   Put simply, we do not understand this argument. An analogous situation is that of non-taxpaying 'stakeholder' pension contributors. They get tax relief on their pension contribution but do not have their personal allowance restricted.

5.1.10 Individuals' tax calculations should pull together all of their sources of income. For example, if HMRC know that someone has a small amount of rental income (which is not enough to require the person to complete a Self Assessment tax return but is instead 'coded out' through PAYE), the P800 calculation at the year end should include that income. If the figure is an estimate, HMRC should flag that this is the case and the individual should advise HMRC of the final figure. This means that the P800 should be comprehensive and it should therefore be possible to calculate the equalisation payment required to put the NPA contributor in the same situation as a RAS contributor. See paras 5.1.2 to 5.1.5 above, where we explain that HMRC is not being asked to pay out the full basic rate relief on NPA contributions – only the balancing amount.

'A claim is necessary' (para 5.15, bullet 3)

5.1.11 A claim is not necessary. Under the 'P800' system for reconciling individuals' tax affairs each year, where a refund is due, HMRC automatically send the individual a calculation of the amount. The individual may then go online to ask for that repayment to be made direct to

their bank. However, if they do nothing, HMRC send them a cheque after 42 days. Indeed, the P800 itself and GOV.UK guidance[9] both say that there is no need to claim.

'A new payment system would be required' (para 5.15, bullet 4)

5.1.12   RAS pension contributors get tax relief on their contribution irrespective of whether they pay tax. No clear explanation has been advanced as to why it is not possible to write the legislation to define any equalisation payment as tax relief, for example in the same way as it is for stakeholder pensions. In that case, the payments could be made through the existing system, as per 5.1.10 above. In any event, the coronavirus situation has demonstrated that HMRC are capable of delivering new payment systems (and at pace).

'There will be a… significant time lag between contribution and bonus' (para 5.16)

5.1.13   This is the same for any repayment of tax under HMRC's systems. Delay is not a reason for inaction.

5.1.14   In fact, in this situation, reconciling the position and issuing a refund after the year end makes it less likely that the payment will have to be adjusted. By the time the year end calculation is carried out, HMRC should have gathered together all of the individuals' income details from data submitted via third parties – the most important being RTI for the low-income people we are referring to – and the calculation should therefore be a 'once and done' reconciliation of the whole year.

5.1.15   The delay would also be helpful in terms of calculating the payment using the correct tax residence status of the individual (i.e. whether using Scottish, Welsh or UK rates), where people have moved during the tax year.

5.1.16   For the – likely rare – occasion in which too much has been paid out, a revised calculation could be sent and processes put in place to collect the debt (which, these being non-taxpayers we are referring to, could not be done via adjusting the individual's PAYE code unless they have started to become a taxpayer at the point of recovery).

'There will be complex issues, for example how it interacts with the… tax and benefits systems' (para 5.17)

5.1.17   National, devolved and local government have all instigated various support measures during the coronavirus pandemic. The tax and benefits treatment of these payments – delivered at speed – has been confusing and complex. However, these problems are not insurmountable and with a relatively minor effort at the outset – HM Treasury and HMRC engaging with other arms of government – the treatment of any equalisation payment could be decided and legislated for.

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[9] https://www.gov.uk/tax-overpayments-and-underpayments/if-youre-due-a-refund

5.1.18   For example, if an individual is due a tax refund relating to employment income, this is to be treated as income for universal credit[10], yet HMRC does not pass details of tax refunds to DWP to be automatically included in benefit calculations.[11] This is already therefore a problem – and one which could be addressed by improved interaction between the two Departments. Payment of a further amount to NPA pension contributors is therefore no different and could be dealt with in the same way.

Delivering this approach

5.1.19   In summary, this approach:

- **puts the onus on HMRC to equalise tax relief for all low earners** – this might come at a cost of implementation, but this would only be a case of adapting existing processes rather than inventing new ones;
- **requires some additional primary legislation, tackling head on the argument that it is not possible to give 'tax relief' to non-taxpayers**, when this is precisely what RAS does. If the equalisation payment can be constructed as tax relief, other arguments about adjusting personal allowances and knock-on effects to benefits fall away – the payment is simply treated as any other tax refund;
- **creates no additional administrative burden on pension scheme administrators, nor on employers** – the solution uses data already passed to HMRC by employers;
- **would need to be clearly communicated to members, but otherwise produces little additional burden.** While we appreciate that this might complicate individuals' tax calculations, the concept 'you pay £10 into your pension and your pot is worth £10. Your friend pays only £8 into their pension, but their pot is also worth £10' is simple enough to convey.

5.2   We also discuss further below how the same principle – of HMRC matching data to individuals' tax records – could be used to give the correct rate of tax relief to people contributing to RAS schemes but who are paying tax at a rate other than 20%.

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[10] Universal Credit Regulations, SI 2013/576 reg 55(4A): *"(4A) A repayment of income tax or national insurance contributions received by a person from HMRC in respect of a tax year in which the person was in paid work is to be treated as employed earnings unless it is taken into account as self-employed earnings under regulation 57(4)."* https://www.legislation.gov.uk/uksi/2013/376/regulation/55

[11] This is not currently done, see Written question 237574, answered 1 April 2019: https://questions-statements.parliament.uk/written-questions/detail/2019-03-27/237574

6   Suggested approach 2 – standalone charge

6.1   *Question 4. We would welcome views on whether equalising outcomes by removing the top-up for non-taxpayers would represent a fair solution to this issue? If possible, it would be useful to understand the impacts on schemes and providers from any such change.*

6.1.1   This would result in a levelling down rather than a levelling up. While the call for evidence notes at para 1.14 that limits on pensions tax relief are out of scope of this review, removing the top up for non-taxpayers would mean having to repeal the £3,600 rule for non-earners receiving tax relief on their pension contributions[12] – originally introduced in April 2001 to complement the stakeholder pension provisions. The alternative would be to have a bizarre situation in which non-earners (or extremely low earners) would be given the top-up relief and then be asked to pay it back. Either scenario would remove an incentive to save for their retirement from those currently benefiting from this relief.

6.1.2   It is interesting to note that the original intention of the £3,600 rule was to allow non-earners to contribute to pensions, with the explanatory notes to Finance Act 2000, Clause 60 and Schedule 13 stating:

> "This opens up pension savings to groups such as carers and parents taking career breaks to bring up children."[13]

6.1.3   While more mothers with dependent children now appear to work than 20 years ago (around three-quarters, as against two-thirds at the start of the century), the statistics indicate that it is still the case that more fathers are in work than mothers (92.6% as against 75.1%).[14]

6.1.4   Consequently, removing the ability for non-earners to contribute to pensions and benefit from tax relief would seem to affect more women than men. This approach would therefore appear to simply swap one social injustice for another.

7   Suggested approach 3 – employers operate multiple schemes

7.1   *Question 5. We would welcome views on whether this approach [employers operating multiple schemes] would:*

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[12] FA 2004, s 190(2)(b), (4)

[13] See National Web Archive, HM Treasury:
https://webarchive.nationalarchives.gov.uk/20000819082558/http://www.hm-treasury.gov.uk:80/financebill/2000/Clause60A.html

[14] Office for National Statistics, Families and the labour market, UK: 2019. See
https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/employmentandemployeetypes/articles/familiesandthelabourmarketengland/2019

> • *reliably mitigate the potential difference in outcome for low earners on a consistent basis*
> • *be a deliverable, affordable and proportionate solution for small employers with a high proportion of low-earning employees*
> • *be appropriate for low earners who are members of defined benefit pension schemes*

7.1.1   We agree with the call for evidence paper at para 5.31 that the administrative burden of this approach renders it unsuitable for all but large employers with significant numbers of low-earning employees.

7.1.2   Moreover, it will not reliably mitigate the potential difference in outcome for low earners, particularly those who have more than one concurrent job or a mix of employment and self employment. In those situations, an individual employer will not have all the information to assess the suitability of each scheme for each employee, as they would only know the individual's earnings in respect of their employment. It might also be unreliable for those with fluctuating earnings, for example when working unpredictable overtime.

8   Suggested approach 4 – mandate use of RAS for defined contribution schemes

8.1   *Question 6. What would be the impacts on schemes and providers of requiring all DC schemes to use RAS? Would this represent a proportionate decision, given potential benefits to some employees and employers?*

8.1.1   This question is not for us to answer, given that we do not have direct knowledge of the burdens on schemes in terms of RAS administration. However, we understand that responses from other members of the NPAG will include evidence suggesting that the cost and burden of moving to RAS 'en masse' is likely to be disproportionate.

8.1.2   This solution would also not be without its own problems – in that it might well 'fix' the issue of the low-paid not receiving tax relief on their contributions but in the process would create other problems.

8.1.3   For instance, those paying at the intermediate rate of tax in Scotland (currently 21%) will get the correct rate of relief via the payroll via NPA. A mass move to RAS would therefore mean that all intermediate rate payers (of whom there were 888,000 in 2018/19[15]) would have to take action to claim their additional relief (although it would mean that all of those paying the Scottish starter rate of 19% would automatically benefit from 20% relief).

8.1.4   To correct this new anomaly, HMRC would – as they should arguably be doing already – need to match pension contributions data to individual records and reconcile where

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[15] See https://www.gov.uk/government/statistics/scottish-income-tax-outturn-statistics-2018-to-2019 - Summary of statistics, Numbers of taxpayers for NSND income bands

additional relief is due. That might be at devolved income tax rates above 20% or indeed be to give relief at rates above 20% across the UK.

8.1.5   Elsewhere in the call for evidence document, the burdens of RAS administration are noted – including for HMRC. The cost of *suggested approach 4* in terms of additional burden for HMRC would therefore seem to be just as great (if not more so) than *suggested approach 1*. Yet it would also create additional burdens for employers and scheme members which we believe would not be the case for *suggested approach 1*, as we have explained in section 5 of this response.

8.2   ***Question 7. Would requiring all new providers of DC pensions to operate RAS represent a fair solution to this issue? The government would welcome views on the longer-term implications of such a requirement, for example whether this would result in existing schemes re-evaluating their arrangements.***

8.2.1   See our answer to question 6 above.

8.3   ***Question 8. Views on whether there would be any benefit in extending RAS to all DB schemes as well as DC schemes would be welcomed. Alternatively, the government is interested to collect evidence on challenges that prohibit such an approach.***

8.3.1   This question is not for us to answer, given that we do not have direct knowledge of the burdens on schemes in terms of RAS administration and how this would impact DB scheme administration. However, we understand that responses from other members of the NPAG will include evidence on this point.

9   Submission of further ideas

9.1   ***Question 9. What changes could be made to the current methods of pensions tax relief that would ensure consistency in outcomes for taxpayers across all aspects of the tax system? If possible, please provide evidence as to how these could be delivered in a proportionate manner by all relevant stakeholders.***

HMRC matching RAS and RTI pension contributions data to all taxpayers' records

9.1.1   As mentioned a number of times throughout this response, the key to individuals getting the tax relief they are due is held by HMRC. We illustrate in the table beneath para 5.1.7 above that HMRC have a wealth of data about individuals and their pension contributions – enough, in many cases, to ensure the right tax relief is given without the individual having to take action.

9.1.2   At present, a Scottish intermediate rate payer in a RAS scheme will have to contact HMRC to get the additional 1% relief they are due on their pension contributions (assuming they do not have to complete a Self Assessment return). Given that the amounts involved may not be large and that there has been no publicity or awareness-raising about claiming this relief, it is questionable how many employees will do this, thus losing out on tax relief that they are

rightly due (however small). In a digital age, and with the data available to HMRC that we have illustrated, contacting HMRC should not be necessary – HMRC are already in a position to make better use of the data they have and ensure consistent outcomes for taxpayers.

9.1.3   Such use of data would indeed seem to be within HMRC sights, given their plans to 'Build a trusted, modern tax administration system'.[16]

Employer education of operating pension deductions from pay

9.1.4   There might be some nervousness surrounding use of RTI data on pension contributions, given that we understand some employers make mistakes in their payroll – for example deducting RAS contributions from employees' pay before calculating tax.[17] Unless this 'upstream' problem is resolved, using pension contributions 'downstream', by pre-populating tax calculations and Self Assessment tax returns, could compound the error.

9.1.5   However, such mistakes can already lead to double tax relief being given (if RAS contributions are treated in the employer payroll as NPA and then the pension scheme reclaims tax relief under RAS). They therefore need to be resolved irrespective of any further use of pension contributions data by HMRC.

9.1.6   Employer education of the problem and checks by HMRC on RTI data submitted (correcting problems where they are found) would help minimise any errors in data and double-counting of relief.

Salary sacrifice

9.1.7   Sitting alongside both RAS and NPA scheme administration is the ability for employees to sacrifice salary in favour of an employer contribution, thus saving National Insurance contributions.

9.1.8   While we make no comment on this as a policy, we would point out that employees of those running salary sacrifice arrangements alongside RAS-based pension schemes might lose out if they make the wrong choice. Again, this is an issue which may impact employees on low incomes, though we do not know the numbers of people earning around or below the personal allowance who might have opted in to salary sacrifice pensions arrangements.

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[16] See HMRC, HM Treasury Corporate Report, 21 July 2020 https://www.gov.uk/government/publications/tax-administration-strategy/building-a-trusted-modern-tax-administration-system – for example, section 5.5: *"Opportunities to modernise tax administration could include… smarter use of data on taxpayers and their activities – pre-population of tax returns, including with data from third-parties – would reduce the need for taxpayers and agents to submit additional information that HMRC either already holds or could verify itself"*

[17] See, for example: https://www.rsmuk.com/ideas-and-insights/employment-tax/spotlight-on-tax-relief-and-employee-pension-contributions

9.1.9   For example, Miss V earns £12,500 a year with ABC Ltd, which offers a salary sacrifice arrangement as part of its RAS-based pension scheme. After being misinformed by a higher-earning colleague that it would save her money, Miss V opts into salary sacrifice. Miss V's pension contributions now cost her more, as she will have lost the benefit of tax relief under RAS, even though NIC has been saved on the amount of salary sacrificed in favour of an employer contribution.

9.1.10   We cannot find much in the way of guidance for employees[18] that warns people against making such a misstep.

9.1.11   It would therefore be of benefit for HM Treasury and HMRC to work with The Pensions Regulator to review guidance and employee risk warnings on this issue.

9.2   ***Question 10. Alternatively, is there a balance to be struck in ensuring consistency in outcomes as far as possible, but prioritising simplicity for individuals? Is there evidence that would support this approach as more likely to build trust and engagement with the pensions system?***

9.2.1   One of the problems with having complexity in the tax system is that if people do not understand, they might fail to do something and get their tax affairs wrong.

9.2.2   In the case of our favoured solution to the issue of low-income NPA pension contributors not getting tax relief – broadly *suggested approach 1* – the calculation of the payment to the individual might well be complex. However, the principle of it can be conveyed in a relatively straightforward manner. And the fact that the calculation is complex should not lead to error by individuals, provided HMRC explain what data they have used to produce the calculation, how the individual can check it and how they can query it if they are not certain or think it is wrong.

9.2.3   In this respect, the Office of Tax Simplification has said:

> "Probably the best route in practice to a simpler tax system is increased digitisation. The OTS illustrates this by the example of a PC: few people know what goes on inside but good interfaces mean it can be a simple machine to use. So it is with taxation: hence the point above about considering compliance aspects early in the process. But the power of digitisation can mask complexity: the OTS has long been keen on the idea of pre-populating tax returns and the measures announced in Budget 2015 point the way towards making the tax system seem much simpler by

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[18] For example, The Pensions Regulator does not seem to offer a standard letter for employees referring to salary sacrifice. See https://www.thepensionsregulator.gov.uk/en/business-advisers/automatic-enrolment-guide-for-business-advisers/8-writing-to-your-client's-staff

linking the information the centre has on taxpayers' affairs and reflecting that back for checking rather than expecting full re-entry."[19]

10   Improving the administration of RAS

10.1   *Question 11. The government would welcome any evidence on whether the RAS system of pensions tax relief administration creates significant additional burdens as compared to net pay, as well as setting out what those burdens are, suggestions for any changes that could be made to ease such issues. In particular, the government would welcome thoughts on the following themes:*

• whether the current system of declarations causes difficulty in claiming tax relief

• any suggestions for practical ways that the earnings limit could be confirmed that would benefit the individual pension scheme member, and

• potential operational changes needed to support a requirement for interim claims to provide relevant details of individual members

10.1.1   This question is not for us to answer, given that we do not have direct knowledge of the issues. However, we understand that responses from other members of the NPAG will include evidence on this point.

10.2   *Question 12. The government would welcome views on whether there are operational changes that could be made to improve the operation of the RAS system and improve member outcomes. Is there evidence that current processes can help to support some employers or pension schemes; or does the paper-based nature of the RAS system create any obstacles in the process for claiming tax relief?*

10.2.1   As mentioned in answer to question 9 above, we believe that HMRC could improve member outcomes by reconciling pension contributions data to individual records and pay tax refunds automatically to (or pre-populate tax returns for) them.

LITRG
13 October 2020

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[19] See OTS Complexity Project paper 'Avoiding complexity: the OTS's lessons learned and some principles', 18 June 2015 - https://www.gov.uk/government/publications/how-to-avoid-complexity-in-the-tax-system