FINAL 4.10.2018

Dear Chancellor,

Automatic enrolment is a policy success story with nearly 10 million people saving into a workplace pension because of its introduction.

The government provides tax relief on pension contributions to help encourage people to save. But more than a million low earners are missing out on tax relief through no fault of their own.

We believe in two principles:

1. The means by which tax relief is paid (net pay or relief at source) should not affect the amount of tax relief paid.
2. Savers should receive this relief automatically, without having to ask HMRC for it.

Why does this issue exist?

There are two ways pension savers can receive tax relief – through either 'net pay' or 'relief at source' (RAS) arrangements.

Under net pay arrangements, the pension contribution is deducted before the tax is calculated. In RAS arrangements, the pension contribution is deducted after tax is calculated and HMRC later send the tax relief, at the basic rate (20%), to the pension scheme.

The vast majority of occupational pension schemes operate on a net pay basis while traditionally contract-based schemes have operated on a RAS basis.

Members of RAS pension schemes who do not pay income tax, typically those earning less than £11,850 each year, are nonetheless, entitled to basic rate tax relief on pension contributions up to £2,880 a year.

However, this tax relief is not available for non-taxpayers in net pay schemes. This means that the lowest earners in net pay schemes are having to pay 25% more for their pensions (by missing out on 20p for every £1 contributed, they need to pay 25% more to achieve parity).

Many are unaware of this, but we urge you to address the situation urgently for these low-paid workers who can least afford the added cost.

Figures from HMRC indicate that in 2015/16, 1.22 million people could have been affected by this issue – that includes those automatically enrolled as well as workers already in occupational schemes.

Somebody earning £11,850, paying auto enrolment minimum contributions, is missing out on £34.91 in the current tax year. By 2020/21, when the personal allowance is expected to have risen to £12,500 (and the minimum contribution rate has also risen to 5%), affected savers could miss out on nearly £65 per year.

HMRC is looking at solutions to resolve an issue which has arisen in RAS schemes as a result of devolved taxation, namely that 21% Scottish taxpayers are missing out on the 1% extra tax relief they are due. We urge government to use this opportunity to put things right for low paid workers in net pay schemes.

To prevent auto enrolment being undermined, it is essential that the government takes decisive action based on the two principles above. This needs a clause in the Finance Bill and utilisation of the system changes that are already underway in HMRC to tackle the devolution problem. We are very happy to work the details through with your HMRC colleagues to make sure all savers are treated equally.

Yours sincerely,

Caroline Abrahams, Charity Director, Age UK

Baroness Ros Altmann, Chair, pensionsync

Troy Clutterbuck, CEO, NOW: Pensions

David Dalton-Brown, Director General, Tax Incentivised Savings Association (TISA)

Anne Fairpo, Chair, Low Incomes Tax Reform Group of the Chartered Institute of Taxation

Helen Hargreaves, Associate Director of Policy, Chartered Institute of Payroll Professionals (CIPP)

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