

Pensions and Savings Team
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

13 October 2020

Dear Sir or Madam

Pensions tax relief administration: Call for Evidence

Thank you for your Call for Evidence seeking views on a range of questions in relation to pensions tax relief administration. I respond on behalf of the Local Government Association (LGA) and the Local Government Pensions Committee (LGPC).

The LGA is a politically led, cross-party membership organisation that works on behalf of 335 councils in England including district, count, metropolitan, unitary, London boroughs and the City of London. There are also 22 Welsh unitary authorities in membership via the Welsh Local Government Association (WLGA). The LGPC is a committee of councillors constituted by the LGA, the WLGA and the Convention of Scottish Local Authorities (COSLA).

This response sets out our technical view, where appropriate, on the questions posed in the Call for Evidence. This response makes no comment on policy regarding current pensions taxation, the rates of pension tax relief or the future direction of policy in this area. I hope the content is helpful; if you have any questions, please do not hesitate to contact me.

Yours faithfully



Jeff Houston
Head of Pensions

Questions raised in the Pensions tax relief administration: Call for Evidence

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

The Local Government Pension Scheme (LGPS) is a statutory public service pension scheme. The decision to deduct member contributions by way of the net pay arrangements was made by the Government. This is most likely because the relief at source (RAS) arrangements were not introduced until 1988, and the LGPS was established in 1922.

Currently, the LGPS regulations prescribe that members who earn less than £14,600, must contribute 5.5 percent of their pensionable pay by way of the net pay arrangements. Members who earn approximately £13,500 enjoy the full 20 percent tax relief on their member contributions and thus only contribute 4.4 percent. Those who earn beneath this figure, see their tax relief reduced proportionately to nil and their contributions increase from 4.4 percent to 5.5 percent (a difference of 1.1 percent).

It is important to note that of the **577,000** individuals with pensionable pay below £12,500 in LGPS employments **507,000 are female** and **385,000 are over the age of 40** both of which may be potential sources of challenge on the grounds of discrimination against protected groups.

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)?

The Local Government Pension Scheme (LGPS) is a statutory public service pension scheme. The decision to deduct member contributions by way of the net pay arrangements was made by the Government. This is most likely because the relief at source (RAS) arrangements were not introduced until 1988, and the LGPS was established in 1922. In 1988, neither scheme administrators nor employers were consulted as to what arrangement should be used thereafter. Consequently, the net pay arrangement continued to be applied, which has led to an inequality in the payment of contributions by those with aggregate earnings beneath the personal allowance.

3. Are there ways that this approach [paying a bonus using RTI data] could be delivered that would not engage the issues identified above, namely the challenges in ensuring consistency across all taxpayers for all aspects of the tax system in a timely fashion, and additional burdens for scheme members and scheme administrators?

Although we are not aware of any alternative approaches, a lot of LGPS employers already operate the RAS arrangement as they have employees who contribute to different pension schemes. Therefore, we do not agree that this would be an entirely new process.

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.

We do not agree with this approach. It would create a further imbalance between those members who enjoy tax relief on their pension contributions and those who do not and would not support the government's policy of encouraging pension saving through automatic enrolment.

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

- reliably mitigate the potential difference in outcome for low earners on a consistent basis

We agree that this solution reliably mitigates 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

We believe this solution to be deliverable, affordable and proportionate for LGPS employers with a high proportion of low earning employees.

The L G P S has 577,000 active members with aggregate pensionable earnings in LGPS employments beneath the personal allowance. When compared with the total number of active members (1.9m) this represents a significant proportion of active scheme membership.

However, having liaised with payroll providers their preference would be to adopt the RAS approach for the entire active membership of the defined benefit LGPS. We consider this approach to be deliverable, affordable and proportionate for LGPS employers, if and only

if, the RAS declaration can be obtained electronically as opposed to the current paper-based solution and that the return of monies to LGPS funds do not lead to cash flow issues.

- be appropriate for low earners who are members of defined benefit pension schemes

We agree that this solution would be appropriate for low earners who are members of the LGPS.

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?

Each LGPS sub-scheme administrator is required to establish by agreement an in-house additional voluntary contribution scheme (AVCs). This is a defined contribution scheme, and contributions are made under the net pay arrangements. If it is determined not to proceed with suggested approach 3, then we do not believe this to be a proportionate decision. This is because LGPS employers will be forced to operate multiple arrangements without solving the tax impact to low earners.

It would also create an additional burden on those members who receive pensions tax relief and contribute to in-house AVCs. This is because they would have their main scheme contributions deducted by way of the net pay arrangements, whilst their in-house AVC contributions would be deducted under the RAS arrangement.

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.

Each LGPS sub-scheme administrator is required to establish by agreement an in-house additional voluntary contribution scheme (AVCs). This is a defined contribution scheme, and contributions are made under the net pay arrangements. If it is determined not to proceed with suggested approach 3, then we do not believe this to be a proportionate decision. This is because LGPS employers will be forced to operate multiple arrangements for future AVC arrangements, without solving the tax impact to low earners.

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.

In terms of administration, we consider this approach to be deliverable, affordable and proportionate for LGPS employers, if and only if, the RAS declaration can be obtained

electronically as opposed to the current paper-based solution and that the return of monies to LGPS funds do not lead to cash flow issues.

The LGPS is one of the largest DB schemes in the world and is the largest DB scheme in England and Wales, with 15,700 employers, 5.9m members and assets of £291bn. A blanket change from the net pay to the RAS arrangement for all active members (approximately 1.9m members) would significantly impact cash flow leading to a detrimental effect on investments. If the operation of RAS was extended to all DB schemes there would have to be a change to the timing by which the scheme received the tax relief from HMRC in order to avoid a significant impact to scheme funding.

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.

A shift in the RAS system that delivers tax relief payments to pension schemes quickly and effectively without the need for individuals to make any form of claim would provide a level playing field of outcomes for all taxpayers. This would also ensure that any future changes to the taxation of pensions would neither have to be linked to income tax rates or require extensive changes to payroll systems.

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?

We believe that tax relief on pensions contributions should be applied consistently across the workforce. Whilst the RAS arrangement does require more interaction with individuals, ultimately this ensures that those with aggregate earnings beneath the personal allowance receive tax relief on pension contributions, this does not happen for those same individuals in net pay arrangements.

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

No comment.

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?

Although LGPS employers do not currently operate the RAS arrangement for deducting LGPS member contributions, we do have some thoughts on chapter 4. The requirement to submit paper-based declarations in 2020 seems archaic. The majority of pension scheme and individual interactions with HMRC (and other Government departments) are done so electronically, it does not seem such a huge leap to extend the RAS declaration to electronic submissions.