EXPLANATORY MEMORANDUM TO

THE REGISTERED PENSION SCHEMES (NET PAY ARRANGEMENTS) REGULATIONS 2026

2026 No. 671

1. Introduction

1.1 This Explanatory Memorandum has been prepared by His Majesty's Revenue and Customs (HMRC) and is laid before the House of Commons by Command of His Majesty.

1.2 This memorandum contains information for the Select Committee on Statutory Instruments.

2. Declaration

2.1 Torsten Bell MP, Minister for Pensions at the Department for Work and Pensions and HM Treasury, confirms that this Explanatory Memorandum meets the required standard.

2.2 Helen Page, Deputy Director for Pensions, Individuals Policy Directorate at HMRC confirms that this Explanatory Memorandum meets the required standard.

3. Contact

3.1 Karen Kirkup at HMRC can be contacted by email at the following address with any queries regarding the instrument: policypensions@hmrc.gov.uk. Alternatively, the department can be contacted by telephone: 03000 512336.

Part One: Explanation, and context, of the Instrument

4. Overview of the Instrument

What does the legislation do?

4.1 Under net pay arrangements, pension contributions are deducted from earnings before income tax is calculated. As a result, individuals receive tax relief only to the extent that they have taxable income.

4.2 Under relief at source schemes, contributions are made from earnings after tax is calculated. The scheme administrator claims basic rate tax relief from HMRC. Individuals receive this tax relief regardless of whether they have an income tax liability. This tax relief is added to their pension.

4.3 Section 193A of the Finance Act 2004 provides for a Low Earner's Pension Payment for certain individuals contributing to a pension under a net pay arrangement. The provision was introduced to reduce disparities arising from differences in pension tax relief between individuals saving under net pay arrangements and those saving under relief at source schemes.

4.4 However, it has become apparent that section 193A does not fully address this disparity. Some individuals who receive less tax relief under a net pay arrangement than they would in a relief at source scheme are not eligible for the Low Earner's Pension Payment under the current rules. This instrument amends section 193A to ensure that these individuals are within scope of the new payment. It also removes the provision treating the payment as taxable earnings. The effect is to place individuals

whose pension scheme is administered under net pay arrangements in a broadly equivalent position to those saving into relief at source schemes.

Where does the legislation extend to, and apply?

4.5 The extent of this instrument (that is, the jurisdiction(s) which the instrument forms part of the law of) is the United Kingdom.

4.6 The territorial application of this instrument (that is, where the instrument produces a practical effect) is the United Kingdom.

5. Policy Context

What is being done and why?

5.1 Under net pay arrangements, pension contributions are deducted from earnings before tax is calculated. This means individuals only receive tax relief to the extent that they have taxable income. Individuals with earnings below the personal allowance, or otherwise with no income tax liability, do not benefit from tax relief on their pension contributions under net pay arrangements.

5.2 By contrast, individuals saving under relief at source receive a top-up into their pension scheme equivalent to basic rate tax regardless of whether they have an income tax liability.

5.3 This difference in treatment means that around one million lower-income individuals in net pay arrangements receive less tax relief for their pension savings than those in relief at source schemes. They may have less take-home pay than an individual in a relief at source scheme saving the same amount into a pension.

5.4 Section 193A (inserted by the Finance (No. 2) Act 2023) introduced the Low Earner's Pension Payment for low earning individuals saving into net pay arrangements. The payment reflects the tax relief they have not received because of the type of pension scheme they are a member of.

5.5 However, at present, section 193A does not fully achieve its aim of ensuring parity between individuals saving under net pay arrangements and those saving in relief at source schemes. Some individuals that are disadvantaged by the difference in tax relief, would not be in scope for the payment. This instrument amends section 193A to address this. It also removes the treatment of the Low Earner's Pension Payment as taxable earnings. This will result in closer alignment of outcomes between individuals in net pay arrangements and relief at source schemes.

What was the previous policy, how is this different?

5.6 The underlying policy objective remains unchanged. The government wants to ensure that lower income individuals in net pay arrangements are not disadvantaged compared to those in relief at source schemes saving the same amount into their pension.

5.7 Previously, the Low Earner's Pension Payment was treated as taxable earnings. This instrument removes that treatment and refines how eligibility and payment amounts are determined, extending entitlement to individuals whose income exceeds the personal allowance, but who nonetheless receive less relief under net pay arrangements. In doing so, it improves parity between the two schemes.

6. Legislative and Legal Context

How has the law changed?

6.1 Section 193 of the Finance Act 2004 provides for tax relief for pension contributions under net pay arrangements by reducing an individual's taxable income.

6.2 Section 192 of that Act provides for relief at source, under which pension contributions are paid net of basic rate tax and the scheme administrator claims the tax relief from HMRC.

6.3 Section 193A was inserted by the Finance (No. 2) Act 2023. It provides for payments to individuals whose total income does not exceed the personal allowance and who are contributing to net pay arrangements. As enacted, it treats those payments as taxable earnings.

6.4 This instrument replaces subsections (1) to (3) of section 193A with a revised framework for determining entitlement to, and the amount of, a Low Earner's Pension Payment. The new provisions require HMRC to compare the income tax relief an individual receives under net pay arrangements with the relief they would have received under relief at source. The difference in those amounts is paid as the Low Earner's Pension Payment. This instrument also provides that any overpayments may be recovered as if they were income tax due, and removes the treatment of the payment as taxable earnings.

6.5 This instrument removes subsections (6) to (8) of section 193A, as they are no longer required.

6.6 This instrument has effect from 14 July 2026.

Why was this approach taken to change the law?

6.7 A legislative amendment is required. Section 193A(9) gives the power to amend or modify that section via regulations. There is no non-legislative alternative.

7. Consultation

Summary of consultation outcome and methodology

7.1 HMRC has engaged with stakeholders, including the Low-Incomes Tax Reform Group and the Net Pay Action Group. Engagement has included communications, customer messaging, and measures to maximise take up.

7.2 Stakeholders are supportive of the policy and the changes made by this instrument, which addresses a long-standing difference in outcomes between net pay arrangements and relief at source schemes for low earners.

7.3 Draft legislation was shared informally with stakeholders for technical comment prior to laying. No drafting changes were identified.

7.4 A formal consultation was not undertaken as this instrument does not impose obligations on scheme administrators or employers. HMRC will identify eligible individuals using existing information from pension schemes and employers and will contact eligible individuals directly to arrange payment.

8. Applicable Guidance

8.1 New guidance will be published explaining eligibility and the payment process.

8.2 Pensions guidance is included in the Pensions Tax Manual[1].

Part Two: Impact and the Better Regulation Framework

9. Impact Assessment

9.1 A Tax Information and Impact Note[2] covering the key aspects for relief relating to net pay arrangements was published on GOV.UK on 15 March 2023 for the Finance (No. 2) Act 2023. It remains an accurate summary of the impacts that apply to this instrument.

Impact on businesses, charities and voluntary bodies

9.2 There is no, or no significant, impact on business, charities or voluntary bodies. This is because HMRC will identify eligible individuals using existing information sources. HMRC will then contact eligible individuals. HMRC will not involve pension schemes or employers.

9.3 The legislation does not impact small or micro businesses. This is because HMRC will identify eligible individuals using existing information sources. HMRC will then contact eligible individuals.

9.4 There will be an administrative impact on HMRC in implementing the arrangements to identify eligible individuals and make the payments.

10. Monitoring and review

What is the approach to monitoring and reviewing this legislation?

10.1 This legislation will be monitored through ongoing engagement with stakeholders, including the Low-Incomes Tax Reform Group.

10.2 The instrument does not include a statutory review clause.

Part Three: Statements and Matters of Particular Interest to Parliament

11. Matters of special interest to Parliament

11.1 This instrument amends primary legislation. The vires under section 193A(9) Finance Act 2004 provide for these regulations to be made.

12. European Convention on Human Rights

12.1 The Minister for Pensions at the Department for Work and Pensions and HM Treasury has made the following statement regarding Human Rights:

"In my view, the provisions of the Registered Pension Schemes (Net Pay Arrangements) Regulations 2026 are compatible with the Convention rights."

[1] Pensions Tax Manual: www.gov.uk/hmrc-internal-manuals/pensions-tax-manual

[2] Tax Information and Impact Note: https://www.gov.uk/government/publications/pensions-relief-relating-to-net-pay-arrangements/relief-relating-to-net-pay-arrangements

13. The Relevant European Union Acts

13.1 This instrument is not made under the European Union (Withdrawal) Act 2018, the European Union (Future Relationship) Act 2020 or the Retained EU Law (Revocation and Reform) Act 2023 ("relevant European Union Acts").