Office of
Tax Simplification

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OTS response to inaccurate press reports regarding the taxation of the state pension at source

The reports of Office of Tax Simplification (OTS) plans to recommend that PAYE tax deductions be applied to the state pension – the so-called 'granny tax 2' – are simply wrong. There are no such OTS plans or recommendations.

It is true that the OTS is looking at the problems pensioners have with the tax system. In the OTS's report published on 6 March (http://www.hm-treasury.gov.uk/d/ots_review_of_pensioners_tax_060312.pdf), one of the problem areas identified was the state pension, stemming from the fact that many do not realise it is taxable at all, the difficulties HMRC have in getting tax collection right and the all-too frequent wrong tax bills that result.

The OTS report noted many possible routes to explore to see if pensioners' tax affairs could be eased. The target is to find a way to get 1.5 million pensioners out of the self assessment system. Bringing state pension into the PAYE system – in the same way as all other pensions, wages and salaries – is a route to explore. But if that route is pursued – others, incidentally, include exempting the state pension from tax – it would not mean a flat 20% deduction from the state pension. That is not how PAYE operates.

PAYE aims to deduct the right amount of tax, which for 5 million state pensioners is nil because of the personal allowance. Were they to have 20% tax deducted, that would mean they were faced with reclaiming tax, and that would bring those 5 million people into the tax system. **This is the complete antithesis of the aim to get 1.5 million people out of tax returns.** Such a route would be a nonsense and will not happen.

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