leading on investments and savings

TISA Budget Submission

March 2014

TISA is a not-for-profit membership association operating within the financial services industry.

TISA's membership comprises over 145 member firms involved in the supply and distribution of savings and investment products and services. These members represent many different sectors of the financial services industry, including banks, stockbrokers, asset managers, insurance companies, fund managers, distributors, building societies, investment managers, third party administrators, consultants and advisers, software providers, financial advisers and pension providers.

Having a legacy of focusing predominantly within the tax incentivised products area, TISA has in recent years moved into the broader savings and investment world, extending our status of 'trusted advisor' to the authorities over a much greater remit. This has been welcomed by our members and the authorities as a natural progression.

TISA has a highly successful track record in working cooperatively with government, regulators, HMT, DWP and HMRC to improve the performance of the industry and the outcomes for consumers. Policy and regulation continues to be the major focus for our members with regard to corporate responsibility.

TISA and its members' remit is evolving into a clearer focus on pro-active consultation in the regulatory world in order to influence policy and associated regulation before its creation, rather than reacting to issued policy directives. This will help to ensure a more considered policy creation from the authorities.

What makes TISA unique is that we cover the entire industry, incorporating cross sector policy, industry and technical expertise. Whilst we maintain a solid partnership with government, the regulators and wider industry, we remain independent and develop neutral views and opinions. This impartiality is reflected in our ability to drive development projects which improves industry performance and puts us in the unique position of being able to constantly challenge the status quo to bring about material improvement. At the forefront in all of our recommendations and actions is to consider national and consumer outcomes.

Re-establishing a Savings Culture

Now that the economic recovery is taking hold we believe it would be timely for the Government to ensure that measures to stimulate consumption-led growth are balanced appropriately with those that will encourage long-term savings.

The UK has one of the lowest savings ratios amongst OECD countries. We face a savings crisis that will profoundly affect consumers who have in successive generations failed to provide for their financial well-being, as well as those who will be expected to bail them out. This presents a major risk to the long term health of the national economy and to social well-being; it is time to recognise that creating a more sustainable culture of personal financial responsibility has become a matter of pressing national importance.

TISA launched the Savings and Investments Policy project in September 2013 with the objective of creating a unified pan industry view of the challenges facing UK consumers' financial wellbeing and the potential solutions to address the key issues.

The project has attracted participation from over 50 organisations representing banking, building societies, life companies, asset management, financial advice, stock broking, asset administration and technology as well as consumer organisations such as the Money Advice Service. In order that the project ensures that the interests of UK consumers are at the heart of any proposals, consumer groups are also actively involved in designing solutions.

In the context of this ongoing work TISA welcomes the opportunity to contribute our emerging thoughts and recommendations to HMT's consideration of the 2014 Budget.

Summary Recommendations

Retirement

TISA strongly supports Auto-Enrolment, the introduction of a flat rate pension, and the increase in the state pension age. These policies provide a strong foundation from which to address the gap in retirement savings and for the further measures we are recommending.

Saving for Retirement

- Conduct a comprehensive review of pensions taxation to establish a cross party consensus on the most effective and fair and economic use of incentives to encourage increased pension saving
- Establish a Workplace ISA Scheme as a credible supplement to traditional pension scheme provision
- Allow trivial commuted pension pots as ISA investments outside of annual subscription limits

At Retirement

- Establish a Commission to conduct a thorough review of de-accumulation options and products, to ensure that they remain relevant and practical for current and future generations at retirement.
- We recommend a range of specific measures that could be implemented in the short term to deliver greater flexibility and effectiveness for income planning in retirement.

Savings

Building on the major success of ISA saving, TISA believes that more can be done to encourage the flexible medium to long term savings that provide resilience during working life and represent a valuable supplement to pension savings. We welcome the Government's decision to allow AIM listed investments to be included within ISAs. This is already delivering greater funding for SMEs and we believe that further changes to allowable investments could accelerate funding to this sector. We are recommending:

- Introduce a new incentivised savings scheme for those on low incomes to replace the Savings Gateway initiative
- Extend permitted ISA investments to include Peer to Peer lending, and Crowd Funding in order to increase the attractiveness of new funding approaches for small businesses in the interests of growth and employment.
- Allow the transfer of ISA assets to spouses and civil partners on death
- Remove inheritance tax liability for ISA assets
- Allow maturing CTF funds to switch automatically to an adult ISA without impacting annual subscription limits
- Enhance the Junior ISA proposition with an element of universality
- Permit direct transfers from SAYE schemes into ISAs without impacting the annual subscription limit
- Allow transfers from unitised Investment Bonds into ISAs without it representing a taxable event

Savings and Investment Policy

Successive generations since the1940s have enjoyed increasing incomes but have also borrowed and spent more and saved less. Over the same period the ratio of years working to years in retirement has shifted dramatically from 3:1 to 2:1 for the current generation. This is unsustainable and implies a risk of increasing dependency on the State. If this is not addressed we can expect that long term damage to the economy will occur through increased taxation to provide state benefits and through reduced consumer spending power. This trend must be addressed by a cultural shift away from debt and spending towards deferred gratification and the re-establishment of a savings habit.

The initial focus of TISA's pan-industry Savings and Investment project has been to identify the key trends and issues facing UK consumers. Findings from this report will be published on March 2014. Key trends that have emerged include:

- UK consumers face financial instability and hardship in the short, medium and long term unless they save more to provide for their financial wellbeing and security.
- Half the households in the UK do not have enough savings to cover an event such as a short period of unemployment or illness without going into debt
- Changes to State and employer pensions, as well as lower investment returns mean that individuals need to save considerably more to have the same level of retirement income as previous generations. This has been exacerbated by historically low interest rates which have impacted heavily on public confidence in annuities.

- The current lack of retirement saving will result in visible national hardship for new pensioners starting around 2035 and will impact subsequent generations
- Increasing longevity adds further pressure as previous generations had 3 years in work for every 1 year in retirement, versus 2 to 1 for consumers born after 1980
- The cost of housing is stretching younger generations' ability to buy a home and this is impacting their ability to save for short term needs and long term retirement
- An increasing dependency on the State is unsustainable and needs to be addressed now

We believe that solutions will require cross political party consensus and a long period of stable legislation and regulation to create greater consumer confidence and encourage a shift back to a culture of savings.

Recognising that consumption has been a major contributor in helping the UK recover from the last recession, increased levels of saving and investment will provide longer term and more sustainable economic growth as it represents a deferral of consumption to a future date while providing greater investment capital for business.

Retirement

During the post-war period we have seen a transformation in the concept of retirement from a very brief period at the end of working life, to a much greater period of two decades or more without earned income. The extended income requirements of longer life have been exacerbated by the greater need for residential care which comes with the increased incidence of health conditions such as dementia which are often associated with advanced old age.

TISA is fully supportive of Government reforms to bring more people to regular retirement savings through Auto-Enrolment, to clarify state pension provision through a single flat rate, and to raise the state pension age further to keep pace with increasing longevity. Important as these reforms are, they still represent only part of the solution and we must continue to look for further measures that will deliver improved prospects of sustainable and adequate retirement outcomes. The Government is for example already aware that the current minimum contribution levels for auto-enrolled pension schemes are inadequate to fund a comfortable retirement for most people and we would therefore encourage further increases to contributions to be fully considered well before the completion of the staging process so that retirement incomes can be brought in line with public expectations.

There are various measures we would recommend to increase the attractiveness of retirement savings:

A comprehensive review of pensions taxation is needed to establish a cross party consensus on the most effective and fair and economic use of incentives to encourage increased pension saving

Although pension tax relief was established on the principle of deferred income, it has in recent times come to be viewed as an incentive for retirement saving. However the effectiveness of tax relief as an incentive, and the fairness of its distribution have been increasingly called into question, and a consensus is emerging that a comprehensive review is required.

It is important nevertheless to recognise that we also need a period of stability on pension taxation, Pension tax relief and allowances have been subject to regular alteration in recent years and this undermines public confidence in pension saving at a time when the industry and policy makers are striving to address the savings gap through Auto-Enrolment. It is essential that any major changes to the current system should therefore receive cross-party support and commitment so that they will be seen by the public to be durable over an extended period.

A Workplace ISA initiative should be established to develop a credible supplement to traditional pension scheme provision with access for other purposes.

Although Auto-Enrolment is proving to be more successful than most had predicted, there are still many individuals who feel that a pension is not right for them. One way to address this is to build on the success and popularity of ISAs to provide a more flexible vehicle for retirement savings that may better address their concerns and requirements.

TISA has created the outline for a Workplace ISA scheme into which contributions from both employee and employer (separate from the individual contribution limit) could be paid. Contributions would be net of personal or corporation tax but would attract NI relief and would be locked in for a certain period to encourage long term savings.

The scheme would operate like an ISA for tax and investment purposes. On reaching the end of the 'lock in' period funds would convert to a standard ISA. The consumer could then leave the funds invested, make withdrawals, transfer funds to a pension scheme or purchase an annuity on the open market.

Trivial commuted pension pots should be allowable for ISA investment outside of annual subscription limits

The principle of trivial commutation is an important facility for those with too small to purchase a useful annuity (typically £10,000). We believe that the principle should continue to be upheld, and that it could be enhanced by allowing trivially commuted sums to be transferred directly into an ISA. This should be outside of the subscription limits, so as to maintain their tax free status, particularly given that a number of trivial pots could nevertheless exceed the subscription limit.

Bearing in mind the Government's work on small pots we believe that this measure would provide a means to encourage ongoing savings whilst enabling small pots to be brought together in a sheltered savings environment.

At Retirement

The annuity industry has found itself under heavy and persistent criticism in recent times. Whilst the industry has raised its standards in response, the value of annuities at their current low rates is still widely questioned, and the potential to default irreversibly to inappropriate products at uncompetitive rates is placing the industry under serious scrutiny.

Whilst annuities are still valuable and appropriate products for many customers, it is time to consider what would be required by way of reform and development to ensure that there is a range of de-accumulation options well suited to the environment and particularly the needs of a growing cohort retiring auto-enrolled savers.

TISA recommends that a Commission be established to conduct a thorough review of de-accumulation options and products, to ensure that they remain relevant and practical for current and future generations at retirement.

With Auto-Enrolment bringing millions of people to pension savings we must look forward to a new generation who will be reaching retirement with pension pots they will want to turn into an income. We might also expect that the environment in which this will unfold will be one of greater diversity in personal circumstances - more extended and second families, complexity of debt and housing, and educational arrangements of adult children, and hence a need for much more flexibility in the way that later life can be financed.

As the demographic shift continues we will find that the most dramatic changes occurring to the numbers of people reaching advanced old age and as a result the need to provide for Long Term Care will continue to increase. This represents a major financial commitment regardless of the welcome reforms announced last year by the Government in response to the Dilnot Report. Long Term Care should be considered an integral aspect of retirement; prefunded care insurance is not a viable market and a thorough review of de-accumulation options and should therefore include flexible and tax-incentivised approaches to residential care funding.

Bearing in mind the current pool of personal wealth existing in property we believe that a review of retirement options would not be complete without consideration of Equity Release products and the opportunity they present in supporting favourable retirement outcomes.

We recommend a range of specific measures that could be implemented in the short term to deliver greater flexibility and effectiveness for income planning in retirement:

- Tax free cash transfers to ISA

  Tax free cash is arguably the best understood aspect of pension tax incentivisation and provides flexibility at retirement to pay off debts. It would be beneficial if it could be invested in an ISA outside of the current subscription limits so as to preserve its tax free status such that it could be used flexibly at a later date as individual's progress through different stages of retirement.

- Income Drawdown Improvements

  Income drawdown rules should be made more flexible so that they can take into account an individual's state of health in the same way as annuities, and the different income levels that are often required as a result of ill-health.

  More generally, greater income flexibility could be delivered through an appropriate increase in maximum income limits on Capped Drawdown, and a reduction to Minimum Income Requirements (MIR) on Flexible Drawdown.

  It would also provide a significant increase to retirement incomes if drawdown limits were brought back into line with annuity market practice by basing them on a combination of gilt and corporate bond investments. Further income improvements could be delivered through other simple measures such as rounding yields up to the next .25% rather than down, basing rate calculations on a six month average to reduce volatility, and introducing a 3% floor on yields used in drawdown calculations to protect consumers against extreme market conditions.

  It would provide further income flexibility and planning choices if part or all of income drawn could then be invested in an ISA outside of the current contribution limits.

- ISA annuities

  It would be a valuable enhancement to the ISA proposition to develop the concept of an ISA Annuity where an income would be purchased from ISA savings. Monthly income would be paid gross rather than net of basic rate tax and there would be no further income tax liability for higher rate taxpayers. We believe that this would afford greater flexibility and financial resilience in retirement for ISA holders and would cement the idea of ISAs as a credible alternative to pensions.

- Allowing annuity income to reduce

As the State Pension Age increases more people may appreciate the ability to draw more income earlier in retirement. Within reasonable limits this should be accommodated within a guaranteed income product as an alternative to drawdown.

- Tax protection for property proceeds used for Long term Care

  With the increasing need for residential care we may expect that individuals will more often wish to dispose of property in a tax efficient manner to provide funding. We believe that it would be beneficial to allow those going into residential care to hold cash from sale of property within a tax free wrapper (similar to an ISA) for the specific purpose of paying fees.

- Early extraction of tax free cash

  Tax free cash could be accessible earlier without crystallising the pension pot to avoid the need for people to convert to income earlier than necessary in order to access capital.

- Tax relief on longevity insurance premiums

  Insurance against advanced old age could be tax-incentivised to provide another option to cover the risk of increasing income requirements in later life as the need for Long Term Care arises.

Savings

Whilst the pressing need to bridge the retirement savings gap occupies much of the public policy savings agenda, it is also crucial for a healthy society and economy to ensure that there is financial resilience during working lives and investment in small businesses.

We recommend:

A new incentivised savings scheme should be introduced for those on low incomes to replace the Savings Gateway initiative.

The Savings Gateway was a well-conceived approach to encouraging saving by those on low incomes. It enjoyed widespread support but when it was shelved in 2010 it was considered to be unaffordable in the economic circumstances of the time. It is a matter of major concern that up to a third of households have little or no savings to cater for emergency requirements and median household wealth (excluding property and pensions) is only £6,600. Four years on we would encourage the Government to develop a replacement scheme which would ensure that a savings habit can take root amongst those of limited financial means who are most vulnerable to life’s adversity without compromising means tested benefits.

Extend permitted ISA investments to include Peer to Peer lending, and Crowdfunding in order to increase the attractiveness of new funding approaches, particularly for small businesses.

We would like to thank the Government for its decision to allow AIM listed investments to be included within ISAs. We can see that AIM stocks have risen by 25% since they were allowed in ISAs and we believe that this effect could be further enhanced by allowing further approaches to investment in small businesses to be included.

As interest rates have been maintained at historically low levels the broad appeal of P2P/Crowdfunding platforms has been increasing, with the market for debt or investment based crowdfunding now standing at over £570m. Individuals are attracted to invest in tangible, green, or alternative opportunities, while the traditional market for business funding has not been able to satisfy the demand for long term capital for SMEs to grow and invest through low cost finance models. We believe that this developing market should be encouraged by allowing investors to earn their returns on a tax free basis.

Allow the transfer of ISA assets to spouses and civil partners on death

At present any investments held by deceased ISA savers lose their tax-free status before they are inherited. Given the average size of those investments relative to the ISA allowance, they are typically placed in ordinary deposit accounts, which are relatively disadvantageous in their tax treatment and interest rates. Often a wife or civil partner will have savings in a husband's name and will lose out significantly.

We believe that ISA savings should be transferable without leaving the ISA wrapper or without affecting the annual allowance. We think this would provide a fairer outcome, especially for women in retirement, and would be a further incentive to save in ISAs.

Remove inheritance tax liability for ISA assets

Whilst ISAs have been a very popular savings vehicle with the public, their exposure to inheritance tends to have an unequal social impact. The 'squeezed middle' may often be placed by virtue of rising house prices, in a position where they are caught by inheritance tax on relatively modest savings. Exemption from inheritance tax would be a major signal that the state is encouraging a culture of individual savings, and we would encourage its economic feasibility to be explored.

Allow maturing CTF funds to switch automatically to an adult ISA.

We would like to see finalisation of the regulations to allow maturing CTFs to transfer into an adult ISA without counting towards the subscription limit. It remains the case that JISAs automatically convert to adult ISAs at maturity whilst this is not currently the case for CTFs. CTFs are still very much a live market and we believe that they should be allowed the same automatic conversion facility as JISA so that equal treatment and certainty will be offered to holders of CTFs.

Enhance the Junior ISA proposition with an element of universality

One of the most compelling features of CTF was its universality, providing normalised access to a savings vehicle for all children regardless of their economic background. We believe this universality has a significant effect on public perception and engagement, and delivers a strong educational message to children as they develop.

It would be a valuable enhancement of the Junior ISA proposition if an element of universality and intergenerational transfer could be introduced so that a small contribution from the state could be made where contributions to a Junior ISA are made by grandparents.

Direct transfers to be allowed from SAYE schemes into ISAs

Where individuals have saved in a tax-advantaged environment we believe that this should be maintained wherever a change of scheme or product occurs. If we are to establish a national savings culture we must aim for administrative simplicity and to remove anomalies that give rise to public scepticism and uncertainty. We should also recognise that as individuals are able to consolidate their savings there is likely to be increased interest in further saving.

With this in mind we believe that employees should be allowed to transfer assets in their maturing SAYE schemes into an ISA without affecting their annual subscription limits.

Transfers from Investment Bonds into ISAs should be allowed without it being a taxable event

TISA believes that unitised Investment Bonds should be transferable without incurring a tax charge in a similar manner to pensions and ISAs. We believe that this would provide a stimulus to the market as well as allowing those who are trapped in old and uncompetitive products to be able to move their funds. In general terms we believe that it would benefit a national savings culture based on simplicity and transferability if such anomalies in the treatment of products could be removed wherever possible.

In Summary

As the UK economy continues its recovery we believe that the opportunity should be seized to embed a savings culture and that the 2014 Budget could be used to make a clear signal of intent. We have proposed a wide range of measures in this paper – some of which could be implemented swiftly and others that involve strategic initiatives.

It may be noted that a number of our recommendations involve the transferability of savings from one scheme type to another. We believe that the complexity of the savings environment and the lack of transferability has been an impediment to public engagement in long term savings and have not been conducive to confidence in a consistent position on saving..

A cross-industry initiative has established TISA Exchange Limited (TeX) to facilitate with common standards, contracts and service levels the electronic transfer of wrappers and assets between fund managers, platforms, wealth managers and any firm which holds assets on behalf of investors. So far the initiative has delivered significant benefits to customers in markedly reduced transfer times and improved efficiencies in the market. Over 85% by value of fund managers and over 90% by assets of platforms are now members, without having to impose new regulations. Instead, this has been an initiative delivered by the market that has encouraged competition and delivered real benefits to customers. We believe that TeX will prove to have a major effect in the development of a savings culture and that it will improve the competitiveness of the market.

TISA would be very pleased to meet with Ministers and officials to discuss and develop the ideas we have proposed and would be very pleased to continue to work closely with HMT to achieve policy objectives.