STRENGTHENING THE INCENTIVE TO SAVE

RESPONSE BY TISA TO HMT CONSULTATION ON PENSIONS TAX RELIEF

Promoting Financial Wellbeing for the UK

TABLE OF CONTENTS

SEPTEMBER 2015

Authors:
Charles McCready – TSIP Programme Director
Adrian Boulding – TISA Strategic Policy Director

1 EXECUTIVE SUMMARY

TISA is pleased to present a set of independently costed, evidence-based recommendations for delivering a more effective approach to incentivising long term saving by individuals that also delivers £2.7 billion of annual savings to the Exchequer. Our recommended approach provides simplicity for consumers and builds upon the success of Auto-Enrolment. Whilst consumers are growing more confident about exercising pension freedoms and choice, they still require strong encouragement to save and the role of the employer will remain critical to success in increasing provision for retirement. The Government provides a valuable benefit to pensions in the form of tax relief and should now position this as matching contributions as this is easily understood by the public and extends a theme already established within Auto-Enrolment.

The Savings and Investments Policy project (TSIP), an unprecedented pan industry group of 50 leading financial services and consumer groups, has spent the past two years researching and developing policy proposals that will enhance savings levels and provide financial security for low and middle income families. We have built upon that work here, plus commissioned additional research to develop solutions that specifically meet the Treasury's objectives for delivering a simple, sustainable, attractive long term solution for pensions. Research indicates:

- The current system of pension tax relief is poorly understood by the general public, provides limited incentive to save and needs to be replaced by a more effective solution
- A new approach needs to be simple to understand and not subject to constant change
- Personal freedoms resonate well with the public in terms of how savings are used but the act of saving itself is far more effective when using mechanisms such as Auto-Enrolment and peer encouragement rather than relying upon individual responsibility
- The concept of a pension ISA strikes an emotional chord with the public but further explanation of this option with test groups results in strong support for the EET system
- A TEE system would reduce the level of pension saving which in turn impacts investment in the UK, economic growth and medium to long term Treasury revenues
- Widespread adoption of a TEE approach would result in limited future tax revenues from retired people at a time they are the biggest users of state benefits
- Running TEE alongside EET creates complexity and costs for consumers, employers and Government
- Moving to universal pension savings of 8% is a step in the right direction but higher contribution levels are needed to provide an adequate income in retirement
- The self-employed have a particularly acute need to increase their provision for retirement and require an incentive specific to their circumstances.

Drawing insight from the research, our recommended proposals are summarised below. These have been reviewed and costed by a respected independent body, the Pensions Policy Institute who indicate that the proposals save the Exchequer £2.7 billion per annum. Recommendations include:

- A single national rate of Government pension matching contribution for DC schemes, with the state providing £1 for every £2 from the employee/individual ("Buy 2 get 1 free")
- Salary sacrifice to be discontinued for the purposes of simplicity and savings to the state
- The lifetime allowance to be scrapped for DC schemes

- Annual allowance limits to be reduced on both DB and DC schemes
- Tax free growth and tax free cash to be retained based on its clarity and popularity
- Employer pension contributions continue to be exempt from NICs
- A new Self-Employed Pension scheme where the state would provide an enhanced level of matching contributions to incentivise a group that has particularly poor savings.

Our research work remains ongoing and we are currently engaged with the Association of Consulting Actuaries, E&Y and Oxford Economics to produce forecasts of both the impact in retirement on consumers of specific savings levels as well as the impact this has at a macro-economic level. This work is due to be completed in October and we will share this with the Treasury at that time. We can however already share that initial projected DC retirement incomes are about half the level that are deemed adequate and that in addition to individuals becoming financially challenged, this will have a negative impact on the economy. This clearly re-enforces the need to encourage greater savings by the public.

We are strongly against the idea of a TEE solution for a number of reasons outlined in this report including our projections that consumers will be worse off – a basic rate tax payer would see their pension pot reduced by 6% according to the current proposal versus a 20% uplift under the TISA proposals – plus OBR projections that tax receipts from retired people under a TEE regime versus the likely costs to the state of public services for these cohorts make the system unsustainable.

We believe we have developed some pragmatic, well supported and attractive proposals that will stand the test of time.

2 EVIDENCE BASED APPROACH

TISA is pleased to respond to this consultation, building upon our extensive two year study of savings and investment in the UK. This work was undertaken by The Savings and Investments Policy project (TSIP), an unprecedented coalition of over fifty organisations representing insurers, fund managers, building societies, banks, platforms, administrators, financial advisers, professional services, trade associations and consumer bodies, united in considering and developing policy measures that should be taken to re-establish a savings culture in the UK. TSIP released a comprehensive research paper in April 2014, followed by a set of policy proposals in March 2015. Work has continued on refining and adding to those proposals, with particular focus on low and middle income earners as the segments of society that most need our support.

One of the key themes in the TSIP work has been the role and design of tax incentives in pension saving and the recommendations we are making are based upon quantitative and qualitative research and analysis. Not only do our proposals represent a consensus amongst a wide range of business across the Financial Services industry but our recommendations are underpinned by:

- Consumer research was undertaken by The Wisdom Council[1] from 3-9 September 2015
- Impact assessment/validation of the TISP model by the Pension Policy Institute
- Forecasting of current pension policy outcomes by the Association of Consulting Actuaries
- Input from industry experts on pensions and savings.

Outputs from this provide a body of evidence which can be found in the appendices. From this work we have drawn the following key findings:

PENSION SAVINGS LEVELS ARE TOO LOW

- With an average 30% replacement rate of pre-retirement income, barely half the OECD average, there is clearly a need to save more to hit the DWP's target of 67%
- The roll-out of Auto-Enrolment will help but at 8% of gross salary contributions, this is well below the projected 12% to 15% needed to provide target retirement income levels
- The band earnings approach to Auto-Enrolment means that the level of contribution is actually substantially lower than the headline 8% suggests.

[1] The Wisdom Council are a team of financial services and consumer specialists who blend engagement, insight and technical expertise with the aim of building meaningful dialogue between customers and financial product providers, re-building trust and ultimately promoting a wider savings and investments culture.

THE CONSUMER PERSPECTIVE

- Retirement is a remote construct for most working age people
- People typically understand much less about pension tax relief than they think – *"Some bits I understand, others bits I know absolutely nothing about,"* Female c55
- They feel detached from their pension and are failing to actively manage those savings
- However, people understand that discipline is needed to save for a pension and are prepared to have that imposed upon them by a third party
- The majority of consumers do not know how much they need in retirement or how much they should be saving.

COMPLEXITY AND TRUST

- The current solution for pensions is considered complex
- There is a belief that the Government is constantly tinkering with the pension system – *"the rules keep changing so it is always difficult to be sure,"* male c60
- Thoughtful design of incentives stands a good chance of increasing pension savings
- It will be difficult if not impossible to deliver a consistent approach across all existing DB and DC schemes.

SOLUTION DESIGN

- The combination of employer, employee and state contributions to workplace pensions is a successful formula to be built upon
- The concept of a pension ISA is popular and strikes an emotional chord with the public, but further explanation of this option results in very strong support for the EET system whereby incentives are received up front rather than in the future
- People favour simple, tangible and stable incentives of a clear contributory nature
- A more effective design of incentives could be afforded within the current cost of pensions tax relief.

THE SELF-EMPLOYED

- The level of pension saving amongst the self-employed is significantly worse than in the employed population
- With 18% of the private sector workforce in self employment, any long term pension solution needs to address this segment, especially those on low and middle incomes
- Whilst the self-employed do have some fiscal benefits, this does not offset the benefits and employer contributions they do not receive.

3 TISA'S RECOMMENDATIONS

TISA's recommendations have been developed by TSIP and benefit from a wide cross section of pan-industry and consumer groups having provided input to the design of solutions. We believe that there are opportunities to change the current pension tax system to create a greater incentive to save for the longer term and benefitting citizens in later life. Our proposals will also enhance the economic health of the UK and reduce the longer term pressures on the public purse.

We believe that the tax system plays a crucial role in maintaining a savings culture and that the system could be designed to provide a more effective incentive. Any changes to the current regime must take account of the crucial role of employers and that the realities of human behavior must be recognised in any future design.

We have undertaken consumer research of the TISA proposals with the public and used this feedback to refine the recommendations.

IT IS THE RIGHT TIME TO REVIEW THE DESIGN OF PENSION TAX RELIEF

The current system has been questioned for some time and its effectiveness as an incentive is difficult to evidence. Repeated tinkering by government has reduced public confidence in pension saving and the majority of people feel detached from their biggest saving asset. Any change therefore needs to be accompanied by a guarantee that there will be stability for a period of time.

There is also a compelling need to greatly improve the level of retirement savings. We currently face a future whereby generations entering retirement will be worse off than the cohorts before them. This will have a wide range of impacts including personal financial hardship, a reduction in consumption that will ripple into the wider economy, a greater dependency on the state and slower economic growth for the UK as a result of low saving rates reducing investment growth.

On a more positive note, Auto-Enrolment has been gaining momentum with 5 million new savers and it provides a platform from which to continue growing both the number of savers and the amount they are saving. Designed correctly, increased levels of pension savings could provide a significant boost to the UK economy.

We propose that due to the complexity of Defined Benefit schemes, the Government considers applying different rules to Defined Contribution schemes, in part to balance out the less generous terms that people within DC schemes receive and also to recognise that the vast majority of people in the private sector are now saving through DC schemes. Our recommendations therefore focus on DC schemes.

AN EFFECTIVE SOLUTION MUST RECOGNISE AND BUILD UPON THE EMPLOYER'S ROLE IN DRIVING SAVING

The Government's recent initiatives for pension freedoms have provided individuals with much greater ownership of how they choose to use their pension savings in retirement. Whilst it is tempting to believe that a new design for tax relief could unleash a latent sense of responsibility and build a saving habit, the evidence suggests that people do not function in that way. Our research indicates instead that employees recognise the need to save for retirement, but would like someone to solve this problem for them, telling them what to do and then making it happen. Without such mechanisms in place consumers are proven to save less. In large part, this is why Auto-Enrolment has been so successful, underpinned by the role of the employer, encouraging and incentivising greater pension saving amongst employees.

THE GOVERNMENT SHOULD MOVE TO MATCHING CONTRIBUTIONS (INSTEAD OF PENSION TAX RELIEF) MAKING THE TAX INCENTIVE SIMPLE TO UNDERSTAND AND ALIGN WITH THE WORKPLACE SCHEMES

A key component underpinning the success of employer pension schemes is the concept of matching contributions. This is easily understood by employees and has been proven to affect their saving behaviour directly. Consumer research points to the attractiveness and immediacy of the employer making contributions on their behalf, and this in turn encourages saving.

We propose that the Government adopts a similar approach in the way it positions tax relief with the public, building upon the way that it already does with Auto-Enrolment – the "cherry on top" model, using the cake analogy adopted in marketing the scheme. We recommend that tax relief is therefore replaced with the concept of matching contributions across all DC pension schemes. This also has the benefit of aligning the employer's and Government's matching contributions and makes it easier for the consumer to understand and value the benefits they are receiving, enhancing the overall incentive to save.

MAKE THE GOVERNMENT CONTRIBUTION EASIER TO UNDERSTAND AND PROVIDE A BOOST TO LOW AND MIDDLE INCOME SAVERS

We recommend that the Government introduces a national flat rate of pension matching contributions for Defined Contribution schemes, adopting a rate that has the state putting in £1 for every £2 put in by the individual from net salary (post income tax and NICs) – or put more simply "Buy 2, Get 1 Free".

Our research, conducted by The Wisdom Council, indicates strongly that consumers are unclear on how much they currently get from Government and that they do not understand either percentages or tax relief. A shift to matching contributions and a simple "Buy 2, Get 1 Free" is a concept they understand and embrace and our consumer research indicates high levels of support for such an approach.

We believe that the benefits of our proposal include:

- Simple concepts with a clear value proposition that encourages greater levels of saving
- This delivers a progressive solution that boosts the savings of low and middle income households, the group needing most support and encouragement
- Higher and additional rate tax payers have sufficient incentive to continue making pension contributions
- Analysis of this proposal by the Pensions Policy Institute has concluded that it would result in a net saving to the Exchequer in the region of £2.1 billion per annum.

As part of the change to a single matching contribution, employers and Government will be required to make changes to payroll and the way that tax relief is applied. We have undertaken analysis of options and suggest the following approach:

- Employees are paid net of tax and NICs on their whole salary
- Any employee contributions into a pension receive a matching contribution at the rate of £2 from the employee matched with £1 from the Government
- Employer contributions are treated as a benefit in kind
- The employer provides a 20% tax credit on any pension contributions made for the employee for basic rate tax payers
- The employer provides a 33.3% tax credit on pension contributions made for the employee for higher and additional rate tax payers
- Employer contributions into the pension would be free of NICs to continue the incentive to make contributions.

In practice, the matching proposal would work as follows:

	Basic Rate Taxpayer	Higher Rate Taxpayer	Additional Rate Taxpayer
Benefit in kind provided by employer	£1.000	£1.000	£1.000
Full tax due on benefit in kind	£0.200	£0.400	£0.450
Tax credit	£0.200	£0.333	£0.333
Tax still payable	Nil	£0.066	£0.116

The outcome of the above is that basic rate taxpayers would see no change to their take home pay when their employer makes a pension contribution into their scheme. For a higher rate taxpayer the employer (using the PAYE system) would show the above figures on the employee's pay slip and take-home pay would be 6⅔p lower for every £1 of employer pension contribution made that month. In the case of an additional rate taxpayer the take-home pay would be reduced by 11⅔p for each £1 of employer pension contribution.

KEEP TAX FREE GROWTH AND TAX FREE CASH

We recommend that the Government continues to offer tax free investment growth within a pension as one of the key incentives for locking up savings for the long term. This also enhances tax revenues at the time that incomes are taken from the pension.

Tax free cash should also be retained based on its clarity and popularity and the considerable issues concerned with retrospection. This will also provide an additional benefit for higher rate tax payers, incentivising them to continue saving through pension schemes which supports the progressive nature of the proposed single rate matching contribution.

REMOVE LIFE TIME LIMITS ON DC SCHEMES AND INCREASE THE INCLUSIVENESS OF AUTO-ENROLMENT TO INCLUDE EXECUTIVE LEVEL EMPLOYEES

There are already concerns that higher paid employees are running the risk of infringing the lifetime allowance. This undermines the powerful 'we're all in' message by pulling executives out of workplace schemes. We want to ensure that these executives, who are typically responsible for defining and deciding on benefits within employer schemes, should be both encouraged and enabled to participate in a single scheme open to all employees, thereby restoring their role as champions of the generosity of the scheme.

We believe that this will have very limited impact on costs to the Exchequer compared with the potential benefits to millions of employees.

PROPOSALS FOR SELF-EMPLOYED INDIVIDUALS

The self-employed represent 15% of the work force. Between 2001 and 2013 their numbers swelled from 3.3m to 4.5m[2]. Only 23%[3] of self-employed people are expecting to fund their retirement with pension savings and of those, the amount that they have saved is half the average of employed peoples' pension pots. Importantly, this sector does not benefit from employer contributions and our research points to this resulting in £91,500[4] being lost in contributions by a third party over their lifetime.

We recognise that this sector receives some benefits with regards tax and NIC treatment, however this is balanced by other benefits from the state that they do not receive and the uncertainty around income.

Our target audience within the self-employed sector are low and middle income earners, who are typically sole traders and do not have a business to sell upon reaching retirement.

[2] Resolution Foundation May 2015
[3] Resolution Foundation May 2015
[4] Office of National Statistics November 2014

Given the size of this sector and the desire on the part of the Government to create a solution that can be implemented and sustained over the long term, we believe that the self-employed also need a solution to encourage retirement saving.

We therefore propose:

- A new Self-Employed Pension scheme with a higher Government matching payment to compensate for the loss of the employer contribution – under Auto-Enrolment the combined Government/employer match is currently 1:1
- Limited to self employed individuals earning up to £30,000 gross per year
- A low annual contribution limit, for instance a target savings rate of 15% of a £30,000 salary suggests a level of £4,500 may be appropriate.

MAKING PENSIONS SUSTAINABLE OVER THE LONG TERM

This is probably the greatest challenge to the Government in seeking to create a solution that balances current fiscal demands with longer term impacts that pensions will have on the Exchequer. These challenges include:

- A desire to reduce the cost of pension tax relief to aid reducing the budget deficit
- The need to incentivise the public to save more and reduce dependency on the state
- The increasing costs of pension tax relief as greater numbers take up Auto-Enrolment and contributions increase towards 8% of employee salaries
- The increasing costs of pension tax relief to take pension contributions beyond 8% to levels that will deliver adequate replacement rates in retirement
- The increasing costs of pension tax relief on public sector DB schemes
- The long term decreasing costs of pension tax relief of private sector DB schemes.

According to estimates by Towers Watson[5], between £4 billion and £5 billion of the £17.1 billion of tax relief paid on employer contributions in 2013/2014 was on contributions related to deficit payments required to meet the pension promises made in earlier years. This should reduce over the medium and long term as these schemes are now mainly closed.

Offsetting this, the Pensions Policy Institute[6] have forecast that if the 9 million people projected to take up Auto-Enrolment at minimum contributions did as expected, that this would cost the Exchequer an extra £4 billion per year. This is based upon the projected costs associated with the TISA solution for pensions rather than the current system. We already know that 5 million of these have already begun the Auto-Enrolment journey and also that some of these costs will be offset by people already in existing pension schemes. Measures are therefore required to tackle these challenges.

KEEP PENSION SIMPLE AND SUSTAINABLE BY DISCONTINUING SALARY SACRIFICE AND REDUCING THE ANNUAL ALLOWANCE

In addition to the £2.1 billion of annual savings that we have identified by switching to "Buy 2 get 1 free", we propose that the Government re-visits salary sacrifice. Discontinuing this arrangement will not affect the target group of low and middle income earners but will impact higher rate tax payers. The work undertaken by the PPI to validate the TISA proposal points towards a potential annual saving of £0.6 billion.

Removal of salary sacrifice as an option for pension contributions will also create a simpler system for both employers and employees.

We note that HMRC's General Anti-Abuse Rule (GAAR) was extended to include National Insurance Contributions in March 2014. Once salary sacrifice of pension contributions to avoid national insurance has been declared as unacceptable tax avoidance by the Government, we believe the existing GAAR powers will be sufficient to stop the practice. Not only do these enable HMRC to collect national insurance on behalf of both employers and employees, they also include the power to impose additional penalties on the

[5] Ending Higher Rate Relief on Pension Savings (Towers Watson) May 2015
[6] TISA Tax Relief Project (PPI) September 2015 – Appendix to this document

employers still offering salary sacrifice and powers to tackle any pension advisers promoting introduction or administration of salary sacrifice.

The Government could also look to reduce the annual allowance. Whilst we have not finished modelling this option, we believe that reducing this to between £25,000 and £30,000 per annum would help to mitigate the additional costs arising from increasing take up and savings levels associated with Auto-Enrolment.

GETTING TO AND GOING BEYOND 8% PENSION CONTRIBUTIONS

There is considerable evidence to suggest that the current level of 8% savings into a pension will not deliver the DWP's target of a 67% replacement rate (including the state pension). Whilst the range of required savings varies greatly, the general consensus is that low and middle income earners will need to save between 12% and 15% of their gross salary, being a combination of individual, employer and Government contributions.

Indeed, the current banding incorporated within Auto-Enrolment means that even the 8% level of whole of salary is not being met. This effect is amplified where people have more than one employment and the banding is applied in each instance.

TISA are still working through solutions and will submit these to Government in due course, however we ask that the current review also consider:

- Additional actions required to support the public through the planned Auto-Enrolment staging contribution increases in 2017 and 2018 to maintain current levels of engagement
- How to increase employee and employer contributions beyond 2018, to target levels of between 12% and 15% of gross salary, which also implies re-visiting the current banding arrangement
- Considering introducing schemes such as "Save more tomorrow" which employ nudge techniques to encourage higher levels of saving.

Whilst the work on this proposal remains on-going in terms of costs and benefits to the state, the rationale is that reducing the dependency of this group on the state in retirement and increasing the potential income tax, plus VAT on consumption will make this option attractive to the Government.

MOVING FROM AN EET TO A TEE REGIME WOULD BE COUNTERPRODUCTIVE

Considerable research has been undertaken into the pros and cons of moving to an ISA model for pensions. We have concluded that this option is less attractive to the public and the nation over the long term.

This chart shows the relative position of different taxpayers under EET, TEE and a 2 for 1 matching system. It looks at the value of the post-tax pension pot generated at retirement by a £100 gross pension contribution from each of the different taxpayer groups. The results are shown as the relative size of the pension pot compared to the outcome for a worker who is basic rate taxpayer both in work and in retirement under an EET system, and so are shown as percentages of this reference group.

Comparison of value of pension pot at date of retirement under different tax treatments:

	Basic rate in work, nil payer in retirement	Basic rate in work and retirement	Higher rate in work, basic rate in retirement	Higher rate in work and retirement	Additional rate in work and higher in retirement
Current EET	118%	100%	100%	82%	82%
TEE	94%	94%	71%	71%	65%
TISA – 2 for 1	141%	120%	90%	74%	68%

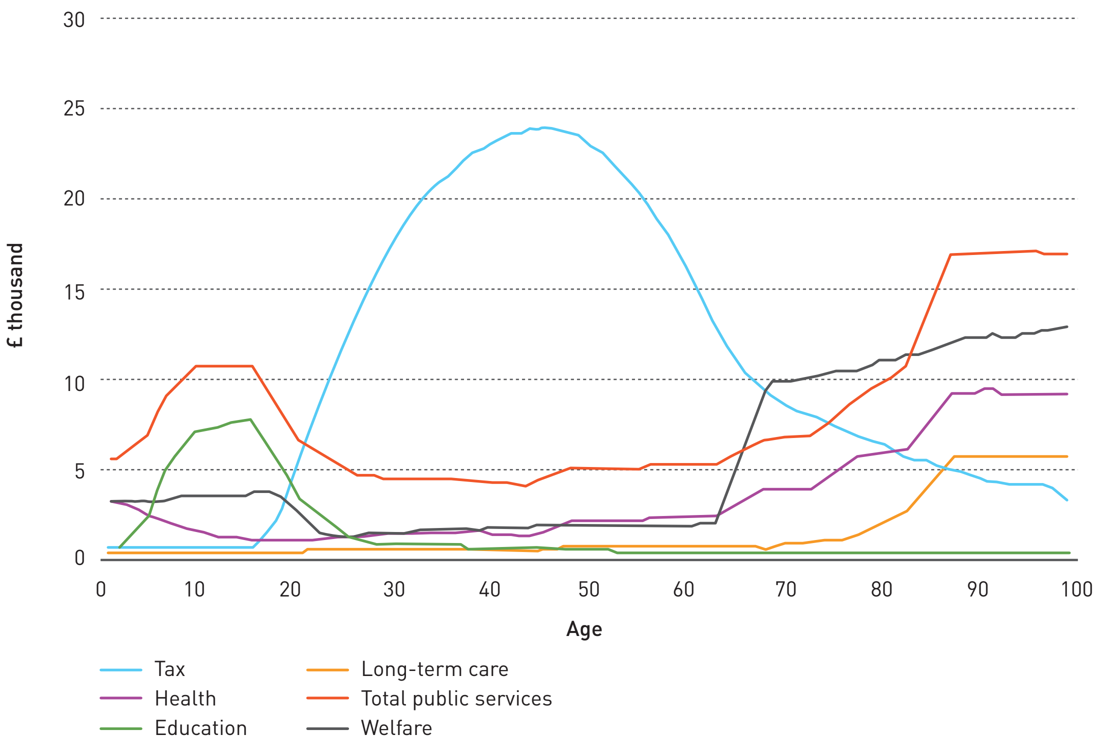
We can therefore conclude that:

- TEE results in considerably lower outcomes and so would require a significant additional Government contribution unless all groups are to be losers
- EET is not as regressive as some people suggest. For the same £100 of gross earnings contributed to a pension plan, lower earners generally do better than higher earners
- A move to 2 for 1 matching would be more progressive, the switch benefitting lower earners at the cost of smaller pensions for higher earners.

We have also set out below five key reasons why a TEE approach would not provide a more beneficial and sustainable approach to incentivising savings:

1. There is no evidence to suggest that TEE would lead to increased pension savings – it destabilises the current momentum for workplace pension saving without offering a clearly superior outcome
2. The removal of taxed withdrawals in retirement reduces the brake on people spending their pension funds too quickly, something that Australia has already experienced
3. It relies on an expectation of consistency of pension policy over a period of decades when this has been conspicuously absent in recent times
4. There would be significant disruption to the saving expectations of individuals and to employers/ providers who have made a major investment in the current pension system and who are accustomed to the flexibility of having both EET and TEE (ISA) saving available to them depending on their circumstances
5. It implies future retiring cohorts would make limited financial contribution to society while consuming high levels of public services, a position which is simply unsustainable.

OBR representative spending/receipts profile



4 TISA RESPONSES TO CONSULTATION QUESTIONS

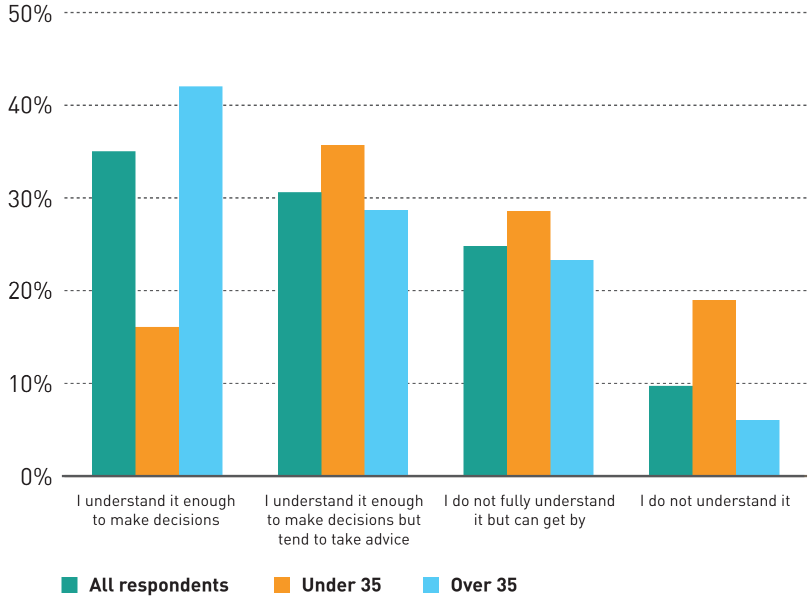
1. To what extent does the complexity of the current system undermine the incentive for individuals to save into a pension?

A significant proportion of the public does not understand how pensions work and how much the Government is giving them. Moving to a single rate of matching contributions is widely supported in consumer testing.

The current system was originally seen to embody the principle that people should be taxed on their income when it was received, rather than when it was earned, but in recent times it has come to be viewed as a deliberate incentive to save and should be judged on its ability to achieve that outcome.

For any system of incentivisation to be effective, it must be clearly understood by the target audience. The evidence provided here[7] and in research undertaken by others demonstrates that the concept of 'tax relief' is poorly understood by the public. We also learned that consumer surveys may be overstating an individual's understanding of pensions; when working with groups of consumers, testing their knowledge in more detail it was demonstrated that they knew even less that they originally believed.

How much do you understand about the current pension system?



[7] TSIP Quantitative and Qualitative Research Findings, conducted by The Wisdom Council from 3-9 September 2015

However, the question of how much this deters the public gets a different response, with older people being less deterred than younger cohorts.

We also have evidence that in the high street consumers are regularly offered incentives that they do understand. These propositions are generally expressed by a simple numerical formula that sets out the benefits the consumer will receive. The lesson to be learned from this is that we should approach pension saving based on the way we know human beings actually behave, rather than believing it is possible to reform behavior to adhere to a detached sense of rationality. This is the basis for Auto-Enrolment and its principle of going with the grain of human behavior underpins its success to date. It is this fundamental lesson that should be at the heart of any changes that are made to the current system of tax relief.

TISA therefore proposes that the Government moves to a system of matching contributions for DC schemes adopting "Buy 2 get 1 Free" whereby for every £2 pounds an individual puts into their pension, the Government puts in £1. Our research points to both the concept of matching contributions and a numerical Government contribution being highly popular.

2. Do respondents believe that a simpler system is likely to result in greater engagement with pension saving? If so, how could the system be simplified to strengthen the incentive for individuals to save into a pension?

Repositioning tax relief as matching contributions and moving to a single universal rate of "Buy 2 get 1 free" presents the Government contribution in a way that will stimulate savings. This should be set within the context of Auto-Enrolment; building on the successful workplace dynamic of employer and peer encouragement engages individuals and embeds a habit of greater pension savings. Reforming the EET system is the most effective approach to take and avoids the pitfalls of a change to TEE.

Retirement is a remote concept for working people, especially for young people. Our research indicates a detachment and lack of ownership regarding their pension and whilst recognising that this is something important for the future, they would prefer someone else to provide them with a solution and then help them take the necessary actions to save.

We believe that the Government should build upon the success of Auto-Enrolment and the important role that employers have to play in encouraging and contributing to building pension savings with employees. Auto-Enrolment captured both the imagination and support of cross political parties and has provided a foundation from which to further secure the financial future of the British public.

Research[8] undertaken by TSIP on the success of pension savings across different countries and schemes points to matching contributions encouraging greater levels of savings. In summary, the introduction of matching contributions was found to increase the level of savings and conversely where matching contributions were removed, pension savings declined. Pension savers were attracted to the immediacy of matching contribution and the adoption of simple numerical matching rates helps to understand the benefit that they will receive.

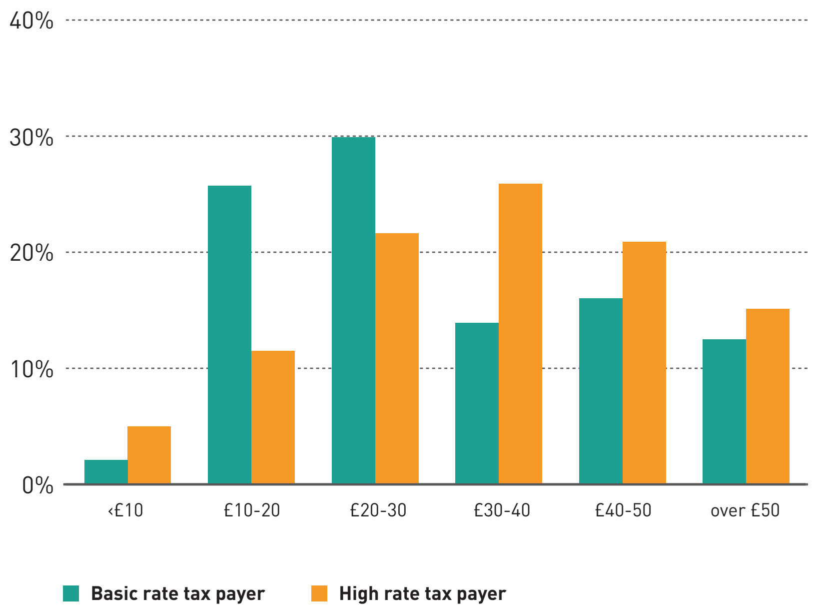
A system of matching contributions has already proven itself in the success of Auto-Enrolment which has been marketed to savers with the simple analogy of a layered cake, and the added Government contribution represented in simple terms as the 'the cherry on top'.

TISA also proposes that for DC schemes, the Government moves from tax relief at marginal rate on pensions contributions to a single universal rate of tax relief presented to savers as a Government matching contribution. Given that research shows that much of the public does not understand

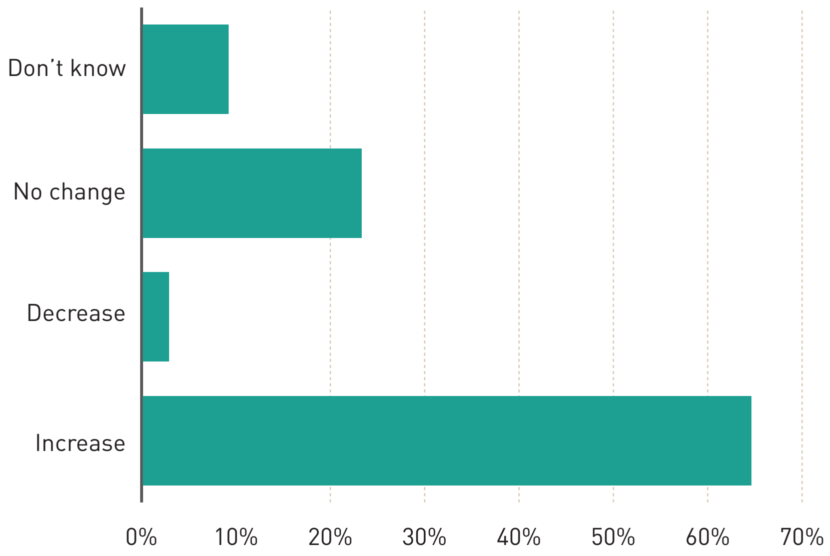
[8] Literature Survey – Evidence on a single rate of tax relief presented as a Government match – See Appendix

percentages, this contribution rate should be in a simple numerical form and we propose "Buy 2 get 1 free", equivalent to a 33.3% pension tax relief rate. The employee would pay tax and NICs at source on their income and any payments into their pension would be matched by the Government with £1 for every £2 the individual paid in.

What is the minimum level of Government contribution that would encourage you to save into a pension – so for every £100 that you contributed, how much would you want the Government to contribute?[9]



Would you increase or decrease your pension contributions if, instead of the current system of tax relief the Government matched pension contributions at a more generous rate with £1 for every £2 you put in?[10]



[9] TSIP Quantitative and Qualitative Research Findings, conducted by The Wisdom Council from 3-9 September 2015
[10] TSIP Quantitative and Qualitative Research Findings, conducted by The Wisdom Council from 3-9 September 2015

Given that the Government has already begun the journey of presenting the public with an easy to understand pension solution within Auto-Enrolment, underpinned by a simple formula of one 4:3:1, there is a good opportunity now to reposition tax relief as matching contributions and at the same time announce a single universal contribution rate. This would then become 4:3:2 (employee, employer, Government) and could be accompanied with a strapline such as "the cherry just got bigger!"

Analysis by the Pensions Policy Institute[11] suggests that based on 2012/13 contributions, this proposals would result in a net saving to the Exchequer in the region of £2.1 billion annually.

We believe that our proposal would have the following benefits:

- Simple concepts with a clear value proposition encourage greater levels of saving
- This delivers a progressive solution that boosts the savings of low and middle income households, the group needing most support and encouragement
- Higher and additional rate tax payers have sufficient incentive to continue making pension contributions.

TISA believes that it would be critical to maintain the role of the employer in encouraging pension saving not just with a congruent matching system but in the manner of its implementation. Employers as well as Government will be required to make changes to payroll and the way tax relief is applied. Our analysis suggests this could be achieved with the following approach:

- Employees are paid net of tax and NICs on their whole salary
- Any employee contributions into a pension receive a matching contribution from the Government at the rate of £2 from the employee matched with £1 from the Government
- Employer contributions are treated as a benefit in kind
- The employer provides a 20% tax credit on any pension contributions made for the employee for basic rate tax payers
- The employer provides a 33.3% tax credit on pension contributions made for the employee for higher and additional rate tax payers
- Employer contributions into the pension would be free of NICs to continue the incentive to make contributions.

We believe it is crucial to ensure that executive level employees are not discouraged from being part of the scheme. These executives are typically responsible for defining and deciding on the benefits within workplace schemes and should be encouraged to act as champions for the scheme and for the 'we're all in' message. This role is undermined where the employer is discouraged by the lifetime allowance from being part of the scheme. We therefore propose that the lifetime limit is removed in DC schemes to ensure their inclusiveness.

We also propose that the Government should re-visit salary sacrifice, recognising its objective of creating a simple, long term, sustainable pension solution. Discontinuing salary sacrifice will not affect the target group of low and middle income earners but will impact higher rate taxpayers. It would also create a more simple system for both employees and employers. The validation work by the Pensions Policy Institute[12] suggests a potential saving of £0.6 billion per annum.

[11] TISA Tax Relief Project (PPI) September 2015 – Appendix to this document
[12] TISA Tax Relief Project (PPI) September 2015 – Appendix to this document

MOVING FROM AN EET TO A TEE REGIME WOULD BE COUNTERPRODUCTIVE

Considerable research has been undertaken into the pros and cons of moving to an ISA model for pensions. We have concluded that this option is less attractive to the public and the nation over the long term.

Five key reasons why a TEE approach would not provide a more beneficial and sustainable approach to incentivising savings:

1. There is no evidence to suggest that TEE would lead to increased pension savings – it destabilises the current momentum for workplace pension saving without offering a clearly superior outcome
2. The removal of taxed withdrawals in retirement reduces the brake on people spending their pension funds too quickly, something that Australia has already experienced
3. It relies on an expectation of consistency of pension policy over a period of decades when this has been conspicuously absent in recent times
4. There would be significant disruption to the saving expectations of individuals and to employers/ providers who have made a major investment in the current pension system
5. It implies future retiring cohorts would make limited financial contribution to society while consuming high levels of public services, a position which is simply unsustainable.

3. Would an alternative system allow individuals to take greater personal responsibility for saving an adequate amount for retirement, particularly in the context of a shift to defined contribution pensions?

Enhancing personal responsibility is a medium to long term goal given the realities of public understanding today. The public needs to grasp why it is important to save and be given the means to make sound financial decisions. Auto-Enrolment continues to be the best way forwards to help the public on the journey to save more and also provides a platform for them to exercise greater personal responsibility when they are ready or able.

The concept of 'personal responsibility' is one that the Government seeks to enhance and is something that TISA supports. However, the reality of public attitudes to savings and pensions remains means that encouraging and empowering them to take greater personal responsibility will take some years to achieve and would require significant effort by the Government to promote financial education and guidance/advice on financial matters.

This needs to be clearly understood when considering the design of any changes to pension tax relief. The inference here is that the saving ethos is as crucial as the outcome – whereas the critical consideration should be that people do in fact save more.

To provide context, recent consumer research[13] indicated that:

- Two thirds of people did not know how much of a pension they needed
- Less than 1 in 5 had planned their pension savings to meet their target retirement income
- Only half knew how much they should be saving even when they had a target retirement income
- 80% did not know if they would have enough to retire on, with more than half of these relying upon good fortune rather than planning to deliver their financial security at retirement.

These results were amplified further with the younger generations having much less understanding of pension planning than the older cohorts, for whom retirement was a fast approaching reality.

[13] TSIP Quantitative and Qualitative Research Findings, conducted by The Wisdom Council from 3-9 September 2015

We also found evidence in our research that people find pensions confusing and that they are detached from their pension even though, aside from their house, this is typically their largest pot of savings. More worrying was the lack of ownership both in terms of personal responsibility in terms of taking the appropriate actions to plan for retirement and the fact that many felt they did not own the assets within the pension.

Any solution to enhance savings levels and an increase in personal responsibility must therefore address these challenges above in addition to the mechanical design of the pension scheme itself.

The concept of 'pension freedom' has been popular in respect of flexibility to draw savings in later life and has engaged consumers, but only for those that are close to retirement and for whom there is some real immediacy and real impact on their lives in the short term. We do not see evidence that this has affected the incentive to save. We currently have a system that places emphasis on guidance at the end of the race (retirement) to tell you how you did and your options, rather than providing the coaching up-front to tell you what the race looks like, how fast you need to go, when you need to start and what happens if you fall.

If the Government wants to develop an enhanced state of personal responsibility, meaning greater engagement, interest and involvement, it implies a sea change in consumer attitudes and will require considerable focus and investment in education to instill the need for saving, then support in the form of advice and guidance to enable the public to make informed financial decisions. The pension system itself is at the end of this chain and will only be fully engaged with once the need and benefits are better understood.

We fully support greater education and advice/guidance and recommend that this is done in parallel with providing pension solutions that encourage higher levels of savings now. This is why we support continuing the approach of Auto-Enrolment as the Government can see the success this has had to date. We currently expect that this will be the most effective mechanism for moving the public towards the level of savings required to provide financial security in retirement and would allow those wishing to take more personal responsibility to save more and apply greater active management of their assets.

By simplifying the system in accordance with TISA's recommendations, we believe the journey to greater personal responsibility will be supported; it makes the system easier to understand and the combined benefits of employer and Government contributions create a greater immediacy and impetus for action.

4. Would an alternative system allow individuals to plan better for how they use their savings in retirement?

The lack of planning today is underpinned by poor understanding and engagement rather than the pension system. We need to tackle this separately from changes to pensions. Greater stability is required as well as a long term Government perspective to ensure that retirement plans made today are not undone by ongoing tax changes.

By way of setting the context to respond to this question, we have repeated some of the key findings below from question 3 from recent consumer research[14] that indicated:

- Two thirds of people did not know how much of a pension they needed
- Less than 1 in 5 had planned their pension savings to meet their target retirement income
- Only half knew how much they should be saving even when they had a target retirement income
- 80% did not know if they would have enough to retire on, with more than half of these relying upon good fortune rather than planning to deliver their financial security at retirement.

Equally the points raised in that response regarding the requirement for greatly enhanced financial education on the need and benefits of saving, plus the accompanying tools to make sound financial decisions with the support of advice and guidance remain entirely valid.

[14] TSIP Quantitative and Qualitative Research Findings, conducted by The Wisdom Council from 3-9 September 2015

In addition to the above, there are other factors that we believe the Government should consider when seeking to help the public plan better for how they will use their savings in retirement.

One big challenge facing consumers is the continual changes to rules applied to their pension savings. Even aside from the challenge of being able to forecast what a DC pension will provide for the given all the variables, the tax treatment of what they can expect to put into their pension or what they will receive continues to fluctuate. Therefore, providing stability of pension and tax rules can provide a little more certainty for the individual.

This is one of the key reasons that we are opposed to changing the system to one based on TEE. Not only does it significantly change the current set of rules, but the longer term viability of the solution points towards a future Government needing to raise more tax to pay for all the public services that older people will be using in future years. People saving through a TEE solution today may therefore find that they need to pay tax again in the future to meet this public service funding gap, resulting in double taxation and impacting on their ability to plan for that future.

Considerable research has been undertaken into the pros and cons of moving to an ISA model for pensions. We have concluded that this option is less attractive to the public and the nation over the long term.

This chart shows the relative position of different taxpayers under EET, TEE and a 2 for 1 matching system. It looks at the value of the post-tax pension pot generated at retirement by a £100 gross pension contribution from each of the different taxpayer groups. The results are shown as the relative size of the pension pot compared to the outcome for a worker who is basic rate taxpayer both in work and in retirement under an EET system, and so are shown as percentages of this reference group.

Comparison of value of pension pot at date of retirement under different tax treatments

	Basic rate in work, nil payer in retirement	Basic rate in work and retirement	Higher rate in work, basic rate in retirement	Higher rate in work and retirement	Additional rate in work and higher in retirement
Current EET	118%	100%	100%	82%	82%
TEE	94%	94%	71%	71%	65%
TISA – 2 for 1	141%	120%	90%	74%	68%

We can therefore conclude:

- TEE results in considerably lower outcomes and would so would require a significant additional Government contribution unless all groups are to be losers
- EET is not as regressive as some people suggest. For the same £100 of gross earnings contributed to a pension plan, lower earners generally do better than higher earners
- A move to 2 for 1 matching would be more progressive, the switch benefitting lower earners at the cost of smaller pensions for higher earners.

Furthermore, the new pension freedoms already provide the ability to draw income and capital from a pension fund from the age of 55, providing both the opportunity to plan better for the future as well as reacting to unexpected events. This further undermines the argument for TEE.

The tax free cash element of the current pension system is also a feature valued by the public. Our research[15] indicates how this money is used today with the main purposes being paying off a mortgage, paying off debt, transitioning to retirement lifestyle and providing an income. We recommend that this feature is retained in the future.

The 'elephant in the room' with regard to pension planning is housing. Many people have been put off saving into a pension by a lack of understanding or trust of pensions and we are all familiar with people that tell us "my house is my pension". In reality, many people planning to create an income from their home in retirement have not taken into consideration the costs of downsizing, the ability to stay within an area that provides them with family and social support and the actual income that they can expect from any capital they manage to release.

We propose that in the future, housing is taken into consideration when planning for retirement and becomes added to the list of assets that financial advisers are qualified to discuss, as well as providing guidance tools that help people make long term financial decisions. In the same way the public does not know how much they need in their pension pot for the sort of retirement they would like, we would assume that this also applies to housing and millions of people are moving towards retirement with no idea if their house will deliver on their expectations.

5. Should the government consider differential treatment for defined benefit and defined contribution pensions? If so, how should each be treated?

TISA believes that Defined Benefit schemes already in existence should not be subject to a new taxation regime for the following reasons:

TISA recommends that DB and DC schemes have different rules going forwards. This rationale for this approach is:

- We favour a single universal matching contribution but applying this to DB brings considerable operational complexity
- The number of DB schemes is in significant decline and half of employer contributions are now in respect of pension deficit reduction rather than future accrual. It would not seem reasonable to change the system while employers are making efforts to make good shortfalls under the current system
- Most DB future accrual is occurring in public sector schemes. In these schemes the cost challenge is primarily the generosity of the employer promise rather than the cost of tax relief, and this has already been addressed by the imposition of cost envelopes following the Hutton review
- Taxpayers in DC schemes would still be called upon to fund a much more generous DB system whilst being unable to participate in it. Different rules are needed in part to balance out the less generous terms people in DC schemes receive.

We therefore recommend that existing DB schemes should be ring-fenced and that the imbalance in the generosity of DB versus DC should be addressed by retaining the annual allowance on DB schemes and that the factor for valuing annual accrual, used to test whether an annual allowance charge is due could be increased (following independent annual assessment). By applying a ring-fence to existing schemes only, any new DB schemes would be required to adopt a tax system equivalent to the £2 for £1 system being created for DC. This is to prevent an arbitrage opportunity where otherwise high earners might create new schemes that count as DB for tax purposes but in reality are largely DC in nature in terms of benefits.

[15] Our Financial Future (TSIP) – March 2014

The table below sets out how we see DB and DC differing in the future.

Pension features

	DC	DB
Tax relief	Universal flat rate matching contributions at 33.3% – "Buy 2 get 1 free"	Tax relief at marginal rate
Employee tax and NICs	Pension contributions paid out of net salary with the Government matching contribution then applied	Pension contributions from gross salary after NICs with 20% tax credit applied and higher bands recovered through tax returns
Employer contributions	• No NICs paid on contributions • 20% tax credit on basic rate contribution for employee • 33.3% tax credit on higher rate contribution for employee	• No NICs paid on contributions • Marginal rate tax relief on contributions for employees
Salary sacrifice	Discontinued	Discontinued
Tax free growth	Yes	Yes
Tax free cash	25% of pension pot	25% of pension pot
Annual allowance	TBD in range of £20k to £30k	TBD in range of £20k to £30k
Lifetime allowance	Removed	£1m

6. What administrative barriers exist to reforming the system of pensions tax, particularly in the context of automatic enrolment? How could these be overcome?

Any reform to the current system risks disruption during the Auto-Enrolment implementation but reforming the EET approach presents no insurmountable issues. However a change to TEE would be a major upheaval.

Automatic Enrolment has been a success story to date and it is very important to continue rolling out this solution at this critical period of its implementation.

The TISA proposal for moving to a single universal rate of matching Government contributions for DC schemes will impact the current arrangements for pension payments handled within payroll. This impacts both employee and employer contributions.

We have considered a range of options and propose that income tax and NICs is applied on gross employee income with pension contributions made from net salary, and the Government then applying the universal "Buy 2 get 1 free" matching contribution.

Employer contributions would be treated as a benefit in kind with a tax credit to compensate for the now taxable nature of the contribution. In the case of basic rate tax payers, this would be a 20% tax credit and for higher and additional rate taxpayers this would be a 33.3% tax credit.

For schemes that currently operate under Pensions Tax Relief at Source (PTRAS), the collection of the Government matching contribution would simply use the existing infrastructure that is used today to collect basic rate tax relief and which is operating irrespective of the tax status of the member. In effect these schemes are already operating a Government contribution match, but at a rate of £1 free for every £4 contributed by members. There will be a greater upheaval for those occupational schemes still using a "net pay arrangement" as these will need to switch to a PTRAS basis. However we understand that many of these schemes are planning such a move already, as the steady increase of the Personal Allowance for income tax over recent years has made net pay arrangement untenable, with low paid members earning under £10,600 p.a. missing out on tax relief altogether.

On this basis we believe that the above changes could be made within the Auto-Enrolment framework with limited disruption to the public, albeit changes will be required by employers and the Government. We do not believe that any of the recommendations we are making would face insurmountable barriers if the implementation is handled within reasonable timescales and with proper consideration of the administrative processes.

Proposed changes to the annual allowance are something that both the financial services industry and Government have managed previously and should not represent significant obstacles.

Abolishing the lifetime allowance for DC removes the need to measure this on the part of scheme administrators and the Government. Most members of the public will never get near the current £1m threshold and this removes a limitation that is typically not applicable to their savings outcomes. However there will be new complexities introduced where individuals have savings in both DB and DC schemes.

A change to a TEE system would represent a major upheaval for Government, employees and employers including significant changes to payroll systems and the development of a new suite of products by financial service firms at a time that there is already considerable change being imposed upon them.

7. How should employer pension contributions be treated under any reform of pensions tax relief?

The role of employers is critical to support a workplace savings culture. In support of TISA's matching contribution reform proposals there are various measures which would sustain and encourage employer engagement.

Any reform of tax relief should recognise the crucial role employers play in incentivising employee pension saving and encouraging it within their workforce. This dynamic should be encouraged by favourable tax treatment of employer contributions when designing the approach to tax incentivisation.

Looking beyond 2018 and the need to continue increasing overall pension contributions to deliver appropriate replacement rates of income at retirement, the employer potentially has a key role to play in gradually increasing their contributions over time. We are assuming that the Government will not provide further incentives beyond those already set out in the TISA recommendations other than acknowledging that increasing employee and employer contributions will impact overall costs to the Exchequer.

We would also like to re-enforce the importance and strength of the 'We're all in' culture which creates a normalisation of the saving habit with participation at all levels in a company.

We have set out below how employer pension contributions would be treated when adopting our recommendation for a single national rate of pension matching contribution incentive for DC schemes with the state providing £1 for every £2 from the employee/individual ("Buy 2 get 1 free").

To support this we are recommending:

- Employees are paid net of tax and NICs on their whole salary
- Any employee contributions into a pension receive a matching contribution from the Government at the rate of £2 from the employee matched with £1 from Government
- Employer contributions are treated as a benefit in kind
- The employer provides a 20% tax credit on any pension contributions made for the employee for basic rate tax payers
- The employer provides a 33.3% tax credit on pension contributions made for the employee for higher and additional rate tax payers
- Employer contributions into the pension would be free of NICs to continue the incentive to make contributions.

In practice the matching proposal would work as follows:

	Basic Rate Taxpayer	Higher Rate Taxpayer	Additional Rate Taxpayer
Benefit in kind provided by employer	£1.000	£1.000	£1.000
Full tax due on benefit in kind	£0.200	£0.400	£0.450
Tax credit	£0.200	£0.333	£0.333
Tax still payable	Nil	£0.066	£0.116

The outcome of the above would be that a basic rate taxpayer would see no change to their take home pay when their employer makes a pension contribution into their scheme. For a higher rate taxpayer the employer (using the PAYE system) would show the above figures on the employee's pay slip and take-home pay would be 6⅔p lower for every £1 of employer pension contribution made that month. In the case of an additional rate taxpayer the take-home pay would be reduced by 11⅔p for each £1 of employer pension contribution.

We also propose that the Government should re-visit salary sacrifice, recognising its objective of creating a long term sustainable pension solution. Discontinuing salary sacrifice will not affect the target group of low and middle income earners but will impact higher rate taxpayers. It would also create a more simple system for both employees and for employers to administer.

We believe it is crucial to ensure that executive level employees are not discouraged from being part of the scheme. These executives are typically responsible for defining and deciding on the benefits within workplace schemes and should be encouraged to act as champions for the scheme and for the 'We're all in' message. This role is undermined where the employer is discouraged by the lifetime allowance from being part of the scheme. We therefore propose that the limit is removed in DC schemes to ensure their inclusiveness.

8. How can the government make sure that any reform of pensions tax relief is sustainable for the future?

It is crucial for public confidence that governments refrain from constant tinkering with the system. Any reform to tax incentives needs to be built on public and stakeholder consensus so that it stands the test of time.

It is essential for savers to have confidence in the pension system. Each time the Government changes tax relief serves to place doubt in the minds of those who are struggling with the financial burden of saving for the long term. So if there is to be a new approach to pension tax relief it should be on the basis that it will be a solution for a generation. Any change needs to accompanied by a guarantee that there will be stability for an extended period of time.

To establish an enduring solution will need a public consensus such as that achieved during the development of the Auto-Enrolment policy. Research suggests that there is already significant consensus regarding the importance of long term saving and the effective incentives and this should form the basis of agreement amongst policymakers and stakeholders which will endure even during times of political change.

The TISA proposals have been validated by the Pensions Policy Institute[16] and can be found in the attached appendix. In summary we found that:

- Introducing the "Buy 2 get 1 free" Government matching contributions for DC schemes would save the Treasury £2.1 billion per annum versus the current system
- Discontinuing salary sacrifice could deliver a further £0.6 billion in annual savings to the Treasury
- Off-setting this, the cost to the Treasury of the additional tax relief payable on the 9 million new savers into pension resulting from take up of Auto-Enrolment on full 8% contributions is £3.9 billion
- The TISA proposals increase this marginally by £0.5 billion to £4.4 billion extra per annum
- This leaves an additional cost of an implemented Auto-Enrolment system of £1.7 billion per annum as opposed to an additional £3.9 billion increase with the current tax regime
- We have not modelled the numbers, but we believe that reducing the annual allowance in line with our recommendations, will help to reduce this funding gap.

According to estimates by Towers Watson[17], between £4 billion and £5 billion of the £17.1 billion of tax relief paid on employer contributions in 2013/2014 was on contributions related to deficit payments required to meet the pension promises made in earlier years. This should reduce over the medium and long term as these schemes are now mainly closed. This will further reduce the additional funding gap set out above.

We are currently working on models that demonstrate the positive impact of the additional pension savings on both the overall economic growth of the country from those savings and the boost to consumption and tax revenues when those savings are spent. We will share this with the Treasury when available in October 2015.

In broad terms, this means that the TISA proposal will be cost neutral to the Treasury, with the benefit that there will be millions more savers who are making larger contributions to their pensions.

MOVING FROM AN EET TO A TEE REGIME WOULD BE COUNTERPRODUCTIVE

A big challenge in predicting the impact of the sustainability of a TEE model is that the industry does not have data on the level of Government contribution that might be considered, nor the treatment of employer contributions, the limits that might be set, etc.

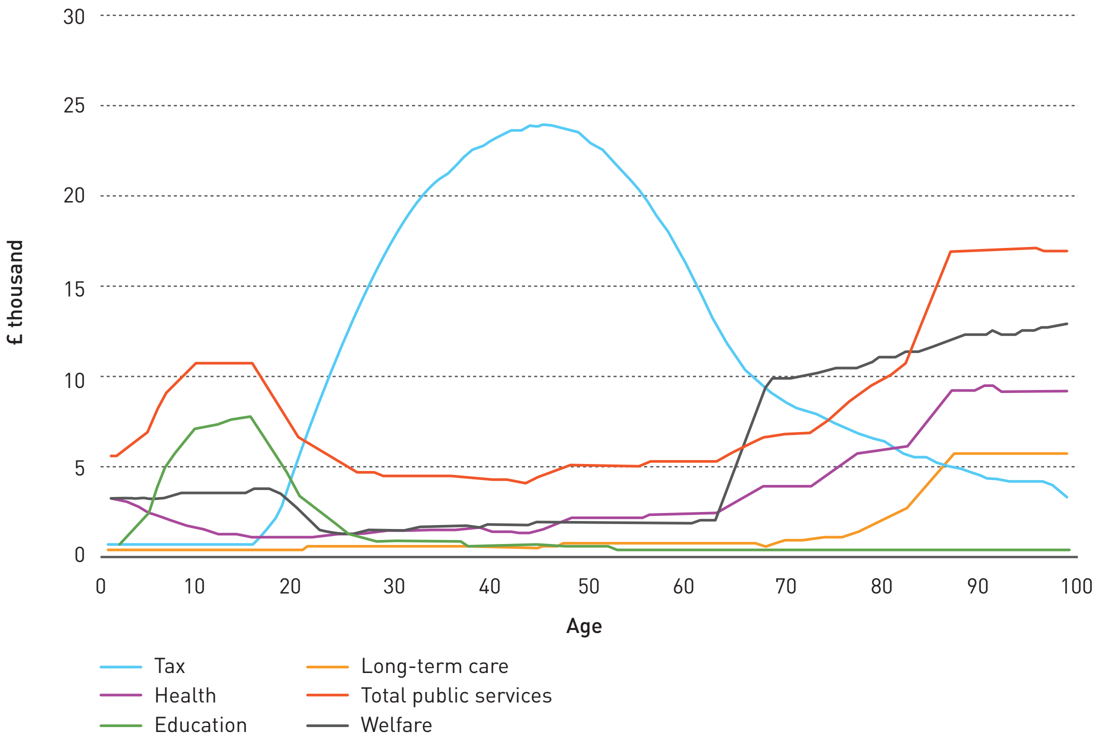
[16] TISA Tax Relief Project (PPI) September 2015 – Appendix to this document
[17] Ending Higher Rate Relief on Pension Savings (Towers Watson) May 2015

Despite this, considerable research has been undertaken into the pro and cons of moving to an ISA model for pensions. We have concluded that this option is less attractive to the public and the nation over the long term.

Five key reasons why a TEE approach would not provide a more beneficial and sustainable approach to incentivising savings:

1. There is no evidence to suggest that TEE would lead to increased pension savings – it destabilises the current momentum for workplace pension saving without offering a clearly superior outcome
2. The removal of taxed withdrawals in retirement reduces the brake on people spending their pension funds too quickly, something that Australia has already experienced
3. It relies on consistency of pension policy over a period of decades when this has been conspicuously absent in recent times
4. There would be significant disruption to the saving expectations of individuals and to employers/ providers who have made a major investment in the current pension system
5. It implies future retiring cohorts would make limited financial contribution to society while consuming high levels of public services which is simply unsustainable.

OBR representative spending/receipts profile



APPENDICES

Appendix A: TISA Background

TISA's role and objectives in developing policy proposals and delivering reform.

Appendix B: Evidence on a Government match

Evidence on a single rate of tax relief presented as a Government match.

Appendix C: Independent Analysis of Proposals

The Pensions Policy Institute's assessment of the cost implications of TISA's proposals.

Appendix D: Consumer Research

Research conducted by The Wisdom Council on public opinion and saving behaviour.

APPENDIX A: TISA BACKGROUND

TISA is a not-for-profit membership association operating within the financial services industry. The focus of our recommendations and actions is improved outcomes for the industry, consumers and the economy.

TISA's growing membership comprises over 150 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 asset managers, insurance companies, fund managers, distributors, building societies, investment managers, third party administrators, consultants and advisers, software providers, financial advisers, pension providers, banks and stockbrokers.

Having a legacy of focusing predominantly within the tax incentivised products area, TISA has in recent years moved into the broader savings and investments world, extending our standing as trusted adviser over a much greater remit.

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 the public. Effective policy and regulation and the creation of efficient industry infrastructure continues to be the major focus for our members. TISA is unique in that it represents the entire financial services 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 improve industry performance and consumer outcomes, putting us in the unique position of being able to constantly challenge the status quo to bring about material improvement.

APPENDIX B: EVIDENCE ON A GOVERNMENT MATCH

Evidence on a single rate of tax relief presented as a Government match

A paper by Adrian Boulding and Imran Razvi for the TSIP project, August 2014

EXECUTIVE SUMMARY

There is evidence from around the world that can inform the TSIP project on the likely behavioural impacts of switching the UK pensions system from marginal rate tax relief to a single rate of tax relief that would be presented to savers as a Government matching contribution.

Matching is demonstrably effective in achieving high levels of participation. Whilst the UK has currently solved the participation question with auto-enrolment, it remains to be seen whether our opt-out rate will remain at around 10% when employee contributions are phased up from the low initial rate of 1%. So a system of Government matching contributions may help maintain the high level of participation currently enjoyed under auto-enrolment.

Contribution levels are surprisingly inelastic to changes in the match level. Introducing a system of matched contributions should not, by itself, be expected to solve the problem of people not saving enough. More generous matching does not feed through to larger contributions.

The level of pension contribution chosen by an individual is often driven by the design of the system, with large numbers of consumers congregating at "kink points" in the system. These "kink points" can be used to drive behaviour, and may need to be deliberately inserted into the tax relief system. For example, a tax system that provided a 1 for 2 Government match up to a 6% workplace contribution, then a 1 for 3 Government match up to a 10% contribution and just 1 for 4 above that up to the £40,000 annual allowance could be particularly effective if the goal was to lift lots of people up to a 6% contribution and to lift higher savers to a 10% contribution. Indeed, our current system that has no real kink points and very high annual allowances of £40,000 for pensions and £15,000 for ISAs may really be missing a trick.

Any contribution increases that come from moving pensions tax relief to a more attractive matching basis will in large part come from reductions in other forms of savings. But that's not as bad as it sounds, as pension savings are much stickier and much less likely to be consumed in the short term than the ordinary savings they may have displaced.

INTRODUCTION

The literature on the effects of employer matching of contributions in pension plans provides some evidence of the likely impact of moving to a single rate of tax relief presented as a Government match of individual contributions. The single rate tax relief matching proposal offers a similar proposition to an employer match – in this case, the presentation of the Government contribution through tax relief as a match can be thought of as a proxy for employer matching in pension plans. As such the evidence on employer matching can therefore be interpreted as providing some idea of the likely behavioural impacts of the proposal discussed in this paper.

THE IMPORTANCE OF TAX RELIEF

Whitehouse (2005) conducted a survey of the different tax treatments of pensions in different countries. Whilst comparisons are complicated by varying levels of Social Security provision, he did find that there was some positive correlation between the generosity of tax relief and the size of private pension funds. He also found that the immediacy of granting the incentive is important, noting a marked reduction in pension saving in New Zealand when that country switched from EET to TTE.

IMF (1998) in a study of OECD countries found not surprisingly that higher income tax rates lead to less saving – if people have less money in their take home pay they have less disposable income for saving.

THE EFFECT OF MATCHING ON PARTICIPATION RATES

A large number of studies consistently find that employer matching of individual contributions increases the rate of participation in a pension plan. Drawing on just a few examples, Papke (1995), Even and Macpherson (1996), Kusko, Poterba, and Wilcox (1994), Basset, Fleming and Rodrigues (1998), Engelhardt and Kumar (2004), and Even and Macpherson (2004) all find that employer matching increases the probability of participation in US 401(k) pension plans[18]. Even and Macpherson find an increase in the probability of participation of 8.8 percentage points if matching is available. Engelhardt and Kumar (2004) find that an increase in the match rate by 25 cents per dollar of employee contribution raises 401(k) participation by 3.75 to 6 percentage points.

EVIDENCE ON THE LEVEL OF MATCHING

There is significant evidence that existence of a match, rather than its level is what matters – that is, providing a match raises 401(k) saving, but an increase in the level of the match rate (conditional on providing a match) does not. Engelhardt and Kumar (2004) find that the estimated elasticity of participation with respect to matching ranges from 0.02-0.07, suggesting that the impact of the match rate on 401(k) participation is quite inelastic. Kusko, Poterba, and Wilcox (1994) find that widely varying match rates at one medium-sized manufacturing firm had little effect on the participation rate of individuals in that firm over a four year period.

Adams, Salisbury and VanDerhei (2012) find, in common with other studies, that matching of contributions increases participation but that increasing the match has little effect on the size of contributions. Interestingly, particularly generous matches may even reduce the level of employee contributions as employees find that their desired level of saving is achieved with a lower employee contribution (in economic terms, the income effect of an increased match dominates the substitution effect of the increase in the match[19]). This effect is particularly marked for lower paid employees.

Other studies corroborate this last finding: work by the Employee Benefit Research Institute (1994), Andrews (1992), Munnell, Sunden, and Taylor (1998) and the US Government Accountability Office (1997) have suggested that, conditional on being eligible for a match, an increase in the match rate lowers 401(k) contributions, which again suggests that employees recognise that a given level of saving can be achieved with a lower employee contribution.

THE IMPORTANCE OF PLAN DESIGN

The work by Kusko, Poterba and Wilcox (1994) emphasises the importance of plan design in determining employee contribution behaviour. In the plan studied in that paper, three-quarters of all employees (and over four-fifths of all contributions) were at one of the so-called 'kink-points' in the plan – contributing nothing, or contributing at the level that obtained the highest level of employer match, or contributing

[18] 401(k) plans are tax-privileged DC pension plans offered in the United States.
[19] In this context, following an increase in the match rate, the income effect reduces an individual's incentive to save, because the same level of individual contribution now earns a larger employer contribution. In contrast, the substitution effect acts in the opposite direction and increases the incentive to save because each employee contribution now attracts a greater match, increasing its value. The empirical evidence is suggesting that at a certain level of matching, the income effect dominates the substitution effect, reducing the overall saving – in order to reach a given level of saving, an increase in the match means the individual can reduce their own contributions.

at the maximum amount allowed under the rules of the plan (which in turn can be dictated by tax rules). In other words, these design features of the plan were very important in determining the contribution behaviour of employees.

The clustering of contributions around such points is important because it suggests that changes in the employer match rate may have little or no effect on these contributions. On the other hand changes in other parameters such as the limit on contributions may have considerable influence on the overall level of saving in these plans.

Madrian (2012) finds a similar phenomenon in her evaluation of the literature on non-financial approaches to increasing individual savings. In particular, the match threshold has a substantial impact on contributions, probably because it serves as a natural reference point when individuals are deciding how much to save and may be viewed as advice from the savings program sponsor on how much to save. When levels of thresholds change, existing plan participants move very slowly to the new kink-points (because of inertia) – but new entrants go to the new kink-points.

A UK PERSPECTIVE – THE SAVINGS GATEWAY SECOND PILOT

The UK Government's pilot exercises on a Savings Gateway offer both a UK perspective on matters and a look at the effect of matching contributions that come from Government rather than employers. However, these were pure savings plans rather than pension plans and of just 24 months duration. Harvey et al (2007) conducted an analysis on the second Savings Gateway pilot which is particularly helpful as this pilot used different incentive levels in different parts of the country.

Comparing Manchester with South Yorkshire, a more generous level of Government match had no noticeable effect on contribution levels, supporting the US evidence that contributions quite inelastic.

Comparing South Yorkshire with East Yorkshire, where the match levels were the same but East Yorkshire were eligible for an account bonus added later on, the extra bonus had no noticeable effect, supporting the US evidence that incentives need to be immediate.

Seven in ten account holders contributed at the maximum match limit, supporting the US evidence that kink points drive consumer behaviour.

There was surprisingly little evidence of either increased savings or reduced consumption. Many participants had funded their Savings Gateway contributions from other savings accounts. Although there was genuine new savings from participants that had no other savings to substitute, and the main way of funding this was found to be reduced instances of eating out.

IMPLICATIONS OF A SINGLE RATE OF TAX-RELIEF PRESENTED AS GOVERNMENT MATCHING

The evidence suggests that the existence of some form of incentive to save in a pension is important, so the first conclusion is that tax relief needs to be maintained in some form. Removing it entirely is highly likely to reduce the level of pension saving. While no one has seriously suggested it should be removed entirely, it should be noted that following the Budget 2014 pensions flexibility reforms, the principle that the granting of tax relief justified the requirement to secure a pension income for life has been weakened. With no restrictions on how DC pension funds are used this principle no longer holds – and in light of this, it is not impossible to imagine future governments questioning whether tax relief on pension savings is still justified.

While the existence of tax relief is important, the evidence suggests that its level is less so. What may be more important is the ease with which the incentive can be understood. A single-rate system on its own would remain opaque and may be less intuitive to the extent that there would be no connection between the individual's marginal tax rate and their rate of tax relief. However, presenting tax relief as matching contributions may lead people to increase their understanding of the value of Government incentives. A single rate matching proposal also has the benefit of appearing simpler than the current system – a simple match compared to differences in the marginal rate of relief paid.

It is highly likely that the behaviour of at least some individuals would change in the face of the altered tax incentives resulting from a move to a single rate of tax relief. A single rate that was set at a level that increased the value of relief to basic rate tax payers, at the expense of higher and additional rate payers may well result in lower levels of saving by the latter two groups as their tax incentives become less attractive relative to the status quo. The evidence on the relative inelasticity of contributions to increases in the level of the employer match suggests that basic rate payers may not necessarily respond to a higher rate of relief by increasing their saving (indeed some of the evidence on the effects of increased matches suggests that they can reduce employee contributions). Therefore, a potential implication of a move to a single rate of tax relief that involves redistribution of relief from higher and additional rate tax payers to basic rate payers is that overall levels of pension saving could fall. Whether or not this reduces the aggregate level of savings depends on the extent to which displaced pension saving finds its way into other forms of saving.

Finally, the discussion on kink points and uncertainty over how individuals will respond to a changed system of tax relief goes to show the limits of tax relief as a mechanism to increase pension saving and the importance of combining attractive tax incentives with other behavioural tools.

BIBLIOGRAPHY

Adams, Salisbury and VanDerhei. Matching Contributions for Pensions Published: October 2012.

Bassett, William F.; Michael J. Fleming; and Anthony P. Rodrigues. 1998. "How Workers Use 401(k) Plans: The Participation, Contribution, and Withdrawal Decisions." Federal Reserve Bank of New York Staff Report, No. 38.

Even, William E., and David A. Macpherson. 2004. Determinants and Effects of Employer Matching Contributions in 401(k) Plans.

Harvey, Pettigrew,Madden,Emmerson, Tetlow, Wakefield : Final Evaluation of the Savings Gateway 2 Pilot, HM Treasury 2007.

IMF 1998. Taxation and the Household Savings Rate : Evidence from OECD Countries, Working Paper WP/98/36.

Kusko, Poterba and Wilcox (1994) : Employee Decisions with Respect to 401(k) Plans. NBER Working Paper.

Madrian, Brigitte C (2012) Matching Contributions and Savings Outcomes: A Behavioral Economics Perspective NBER Working Paper No. 18220.

Munnell, Sundén, and Taylor US Social Security Bulletin, Vol. 64 No. 3, 2001/2002 What Determines 401(k) Participation and Contributions?

Papke, Leslie E., and James M. Poterba. 1995. "Survey of Evidence on Employer Match Rates and Employee Saving Behaviour in 401(k) Plans." Economic Letters 49: 313-317.

Whitehouse, Edward. 2005. Taxation: The Tax Treatment of Funded Pensions. World Bank, Washington, DC. © World Bank.

APPENDIX C: INDEPENDENT ANALYSIS OF PROPOSALS

PENSIONS POLICY INSTITUTE
PPI

TISA TAX RELIEF PROJECT

INTRODUCTION

In the Budget of 8 July 2015, the Chancellor announced a consultation into the use of tax relief to "strengthen the incentive to save" for retirement. TISA asked the PPI to assist them in calculating the impact on the cost to the Treasury of a proposal for a new tax relief system that they had conceived. The TISA proposal consists of the following:

- 33% tax relief on all employee contributions to pension schemes
- 20% tax relief on employer contributions in respect of basic rate taxpayers
- 33% tax relief on employer contributions made in respect of higher or additional rate taxpayers
- Abolish salary sacrifice
- The changes to the system apply to Defined Contribution (DC) schemes only.

This note sets out the impact on the Treasury if the above proposal had been in place in the tax year 2012/13.

The analysis presented in this note uses the methodology presented in the PPI report *Tax relief for pension saving in the UK*[1]. In particular for the purposes of this note we keep **net contributions constant for defined contribution pension** schemes. In deciding how to keep contributions constant, the characteristics of the different types of pension schemes were considered.

DEFINED CONTRIBUTION PENSION SCHEMES

Defined contribution pension schemes do not have funding targets, there is therefore no need to maintain the level of contributions being paid into the pension scheme. Instead it was assumed that employees would be interested in maintaining the same level of take-home pay after making pension contributions into a defined contribution pension scheme. This means keeping the same level of net contributions, and allowing the impact of a change in the tax relief offered to fall on the gross contribution to the scheme.

For the split between Defined Benefit (DB) and DC pension schemes we have used the split that was assumed in TISA's own calculations that were sent to the PPI for validation. That is that approximately 40% of occupational pension contributions are in respect of DC pension schemes, and that all of contributions to personal pensions are to DC schemes.

[1] http://www.pensionspolicyinstitute.org.uk/uploadeddocuments/20130715_Tax_Relief_for_Pension_Saving_in_the_UK.pdf

RESULTS

Table 1 shows the distribution of tax relief to defined contribution pension contributions in the 2012/13 tax year under the existing tax rates. The total cost to the exchequer of tax relief on contributions to DC schemes was around £13.5 billion, of which £10.1 billion was in respect of employer contributions and £3.3 billion was in respect of employee contributions.

Basic rate taxpayers receive 27% of the tax relief while making 51% net of contributions. Higher rate taxpayers receive 55% of tax relief while making 39% of net contributions. Those who pay additional rate tax receive 17% of tax relief and make 10% of net contributions.

Table 1: Distribution of tax relief in 2012/13 (£billions)

Tax band	Tax relief	Contributions	Total Contributions
Basic Rate	3.7 (27%)	14.8 (51%)	18.5 (44%)
Higher Rate	7.5 (55%)	11.2 (39%)	18.6 (42%)
Additional Rate	2.3 (17%)	2.8 (10%)	5.1 (12%)
Total	13.5 (100%)	28.8 (100%)	42.3 (100%)

Table 2 sets out the distribution of tax relief in the 2012/13 tax year if tax relief were to be awarded at a flat rate of 33% on employee contributions, and at 33% for higher and additional rate taxpayers, but 20% on basic rate taxpayers for employer contribution. The total cost to the exchequer of tax relief on contributions to DC schemes would have been £11.4 billion, a reduction in cost of £2.1 billion.

Table 2: Distribution of tax relief in 2012/13 assuming TISA tax relief proposals (£billions)

Tax band	Tax relief	Contributions	Total Contributions
Basic Rate	4.5 (39%)	14.8 (51%)	19.3 (48%)
Higher Rate	5.5 (48%)	11.2 (39%)	16.7 (44%)
Additional Rate	1.4 (12%)	2.8 (10%)	4.2 (10%)
Total	11.4 (100%)	28.8 (100%)	40.2 (100%)

Under the modelled reform option, basic rate taxpayers receive 39% of the tax relief while making 51% of net contributions. Additional rate taxpayers receive 48% of tax relief while making 39% of net contributions. Those who pay additional rate tax receive 12% of tax relief and make 10% of net contributions. This represents a shift of tax relief to the basic rate taxpayers, from higher and additional rate taxpayers.

REMOVAL OF SALARY SACRIFICE

Salary sacrifice enables employees and employers to take advantage of a quirk of the National Insurance system, because employer contributions to a pension scheme are not subject to National Insurance but employee contributions from salary are. So an employee gives up part of their salary, and an equal amount is made as an employer contribution.

Abolishing Salary Sacrifice would have the effect of moving those contributions from employer contributions, back to being employee contributions, where they would be subject to NI contributions from the employer and employee, and also, under the TISA proposal, subject to different tax relief treatment for basic rate taxpayers. It is assumed that 30% of all employee contributions are made in the form of salary sacrifice.

Table 3 sets out the distribution of tax relief in the 2012/13 tax year if Salary Sacrifice were abolished, in addition to the adjustments to tax relief on contributions set out in Table 2. The total cost to the exchequer of tax relief on contributions to DC schemes would have been £11.7 billion, an increase to the cost of £0.3 billion.

Table 3: Distribution of tax relief in 2012/13 assuming TISA tax relief proposals and abolishment of Salary Sacrifice (£billions)

Tax band	Tax relief	Contributions	Total Contributions
Basic Rate	4.8 (41%)	14.8 (51%)	19.6 (48%)
Higher Rate	5.5 (47%)	11.2 (39%)	16.7 (41%)
Additional Rate	1.4 (12%)	2.8 (10%)	4.2 (10%)
Total	11.7 (100%)	28.8 (100%)	40.5 (100%)

But there is also an increase in NI contributions received by the State to offset this cost. Table 4 sets out the impact on NI contributions as a result of abolishing Salary Sacrifice.

Table 4: Distribution of impact on National Insurance Contributions of abolishing Salary Sacrifice (£billions)

Tax band	Increase in salary	Employer NICs increase	Employee NICs increase	Total NICs increase
Basic Rate	2.04	0.28	0.24	0.53
Higher Rate	1.73	0.24	0.03	0.27
Additional Rate	0.57	0.08	0.01	0.09
Total	4.3	0.6	0.3	0.9

The measure might raise revenue for the government at around £0.9 billion.

Taking this all into account, the TISA proposal results in a net saving to the government of around £2.7 billion; consisting of a £2.1 billion saving on changing the contributions and a net £0.6 billion saving from abolishing salary sacrifice.

BEHAVIOURAL IMPACT

The PPI report *Tax relief for pension saving in the UK* considered the impact on contributions if there were a change in savings behaviour as a result of a change in the amount of tax relief offered on pension contributions. This is intended to allow for the fact that a positive change in the return on contributions may induce people to save more in their pension. For example, basic rate taxpayers may be expected to save a bit more, while higher and additional rate taxpayers may save a little less.

In order to reflect this in the distributional analysis for the PPI report, assumptions regarding 'pension saving elasticity' are required. Using research by the ABI it was possible to estimate savings elasticities of pension saving, to both existing savers, and the inducement to start saving to those who do not currently save. See Annex 7 of *Tax relief for pension saving in the UK* for more information.

Using the same methodology as the PPI tax relief report, the results in Table 5 set out the impact on the cost of tax relief of a change in the behaviour of savers in response to the change in the tax relief. In addition, the analysis varies the power of the behavioural impact; what would happen if the behavioural response was 50% less, or 50% more than the standard assumptions. This does not allow for the salary sacrifice abolishment.

Table 5: Impact of behavioural changes on cost of tax relief in under a 33% flat rate tax relief system (£billions)

Tax band	Tax relief assuming TISA relief proposals	Tax relief (50% of behavioural impact)	Tax relief (100% of behavioural impact)	Tax relief (150% of behavioural impact)
Basic Rate	4.5	4.5	4.6	4.7
Higher Rate	5.5	5.2	4.9	4.6
Additional Rate	1.4	1.2	1.1	0.9
Total	11.4	11.0	10.6	10.3

AUTOMATIC ENROLMENT

We used the government figure that Automatic Enrolment will lead to around an additional 9 million people saving and used the Wealth and Assets Survey data to identify the distribution of people who would qualify for automatic enrolment. We have made the assumption that these 9 million people all contribute at the minimum level. That is, the employee contributes 5% of band salary and the employer contributes 3% of band salary.

COST TO GOVERNMENT UNDER THE CURRENT SYSTEM

Applying the current tax relief system to the resulting distribution of people suggests that the Exchequer cost of tax relief on the employer and employee Automatic Enrolment contributions would be around £3.3 billion in 2012/13 earnings terms.

Automatic enrolment legislation requires contributions of 8% of band salary with at least 3% of which being paid by the employer, it does not stipulate how the remaining 5% of contributions must be made. It could therefore be subject to salary sacrifice on those 5% of contributions.

If all individuals who are automatically enrolled were to take part in salary sacrifice, it would lead to a cost of around £2.0 billion in lost NICs. Assuming 30% of employee contributions would be salary sacrificed, this would lead to a cost of salary sacrifice of £0.9 billion.

The total cost of the automatically enrolled individuals under the current system would therefore be around £3.9 billion.

COST TO GOVERNMENT OF THE TISA PROPOSAL

Under the TISA proposal where that employees receive a 33% flat rate of tax relief on employee contributions, higher and additional rate taxpayers receive tax relief on employer contributions restricted to 33%, while tax relief on employer contributions to basic rate taxpayers remains at 20%. This leads to a cost of tax relief of £4.4 billion.

The TISA proposals would abolish salary sacrifice, there is therefore no cost of lost NICs. The total cost of the automatically enrolled individuals is therefore around £4.4 billion, an increase of £0.5 billion on the £3.9 billion under the current system.

The impact of the restriction on employer contributions to higher and additional rate tax payers, beyond the impact of the flat rate on employee contributions, is not very large. This is because the employer contributions are the smaller share of AE contributions, and most AE people are likely to be basic rate taxpayers, rather than higher and additional rate taxpayer. This limits the scope of the restriction as a cost control measure on AE contributions.

APPENDIX D: CONSUMER RESEARCH

THE WISDOM COUNCIL

Rebuilding trust through customer engagement

OUR GOAL

To rebuild trust in Financial Services

HOW

Working closely with firms to:

- Build better connections with their customer
- Deepen understanding
- Give their customers a strong voice

"We work with firms who want to engage actively and positively with their customers."

TSIP QUANTITATIVE & QUALITATIVE FINDINGS, SEPTEMBER 2015

RESEARCH OVERVIEW

Quantitative – To give a robust, statistically viable basis to the research

- Sent to over 1,000 consumers from all segments of the UK Saving & Investing population
- Total sample of 290
- Sample aged 18 –75 all "pre-retired".

Qualitative – To add further deeper colour and insights to the output from the quantitative work

- 2 x focus groups
- 1 x Older group – mix of income, age and background
- 1 x Young professionals... all financially sophisticated and higher rate tax payers – now or near future.

OVERALL QUANTITATIVE & QUALITATIVE SUMMARY

RETIREMENT

- Retirement is a remote construct for working people:
  - Retirement is normally seen as/talked about as being a long way off… until suddenly it is just round the corner
  - Although most people still see retirement as an end to working… professionals are increasingly seeing retirement as a glide path rather than a full stop… cutting back on working, working to their tempo, working on things they want to work on etc.
  - It is a major life change and many do not like to think of themselves as becoming a retiree with the terms pertaining imagery.

47% do not have a specific period in mind for retirement.

- Pension comes with all sorts of negative baggage as a term:
  - Pension is old –versus investments. It is an old term.
  - Pensioners are clearly old… and past it. Being a pensioner is not seen in a positive light
  - Pensions are intimately associated with the State Pension for the young… with consequent associations.

75% see retirement as not working or do not intend to work when retired.

OWNERSHIP

- Not only is there a remoteness between most working people and the concept of pensions/retirement, there is an actual perception of lack of ownership of pensions themselves
- Consumers do not feel they own pensions and pension pots are not 'owned' in the way that they feel they own their bank account, their mortgage or other investments
- Pensions lack immediacy and tangibility. People know they get their yearly pension update but it lacks a sense of personal ownership
- This can make pensions less attractive and motivating and provide another reason/excuse for inertia and disinterest.

"It's not really mine until I start drawing it."

PENSION PLANNING

- There is very little active planning in terms of retirement or pensions – particularly among younger people who have other demands on money – home, children, enjoying life, servicing debt etc.
- Those with an occupational pension may add voluntary contributions but rely heavily on the occupational pension scheme... so what they get from this source is what they will just have to live on.

38% believe they know the size of the pension pot they need to fund the lifestyle they would like.

Only 18% believe they have planned their pension/ investments sufficiently to achieve the pension pot they require.

53% do not know how much they should be saving/ investing to achieve the required pension pot.

Of those planning to retire within 10 years, only 27% believe they have enough money to meet their plans.

PENSION KNOWLEDGE

- Knowledge of pensions is actually pretty hazy although most claim they do understand the current pension rules
- Most confusion revolves around tax and tax relief
- Distinct lack of knowledge about maximum annual contribution and maximum lifetime allowance
- Perception that pension rules will change... and potentially change a lot in the working lives of the young.

Almost everyone thinks they know enough about pensions to get by.

72% claim that the complexity of the current system is no deterrent to saving.

35% feel they know enough to make decisions without advice.

COMMUNICATION

- Pensions can be motivating
- When laid out simply the basics of pensions are relatively easy and straightforward
- People complain that most pensions communications lack clarity and motivational affect
- This is partly a 'get out' – that 'blames' their lack of action and interest in pensions on others
- But many of the issues surrounding pensions are communication issues.

Wording matters:

There is a clear emotional difference between tax relief and a Government contribution (like the employers contribution).

Government contribution appears to be more motivating.

POLICY PROPOSALS – LEVELS OF INCENTIVES

- When presented as tax relief, higher rate tax payers and aspiring higher rate tax payers expected to get more relief/contributions from the Government
- However, when presented with matching options, those earning over £40k p.a. were unlikely to change their contributions even at lower levels of matching.

57% of those earning <u>under</u> £40k thought the minimum level of Government contribution to encourage saving was between £10-30 for every £100 saved.

41% of those earning <u>over</u> £40k thought the minimum level of Government contribution to encourage saving was between £30-50 for every £100 saved.

POLICY PROPOSALS – EMPLOYER SCHEMES

- The employers 'contribution is a major driver... the more the employers' contribution the more motivating for the individual to contribute
- Simplicity and transparency are key to the matching contributions
- Auto-enrolment is seen as a major positive step:
  - — Makes pension saving easy, straightforward and effortless
  - — Pension payments are not noticed
  - — Removes the need for individual action/decisions
- For the younger age group, an employee scheme was the principle reason they had pensions and employee matching the main motivator for their own contributions
- There was limited evidence of support for the idea that the self employed or those without company schemes should get higher Government contributions.

90% were prepared to contribute 8% of their pay if the employer or Government put in another 7%.

73% believe that it should be compulsory to save into a pension.

"If I hadn't joined a company with a pension scheme I probably would not have a pension."

WHEN TO TAX AND LIMITS

- The quant questionnaire showed that people preferred to be taxed now and receive it tax free later
- It was perceived as giving more flexibility
- In the discussion groups, on balance people preferred retaining the current system
- £250,000 and 25% tax free was seen by the majority as fair
- The Lifetime limit and Annual allowance are remote for most people and do not deter – although:
  - — For aspiring young, £1m was not seen as sufficient to meet with goals
  - — There was little understanding.

"I didn't know anything about the 25% tax free amount."

Only 12% said the lifetime limit deterred them from saving.

68% preferred to pay tax now and then take it out tax free.

PENSION RULES IN GENERAL

- People want rules… that stop them making bad decisions or being indisciplined when it comes to pensions
- There is a debate around using pension money to get on the property ladder… given that many see their home as a potential part of their pension through downsizing
- There was some belief that being able to access your pension before 55 in the extreme case of terminal illness would be fair
- But by and large people want pensions for retirement only.

42% of under 35's and 37% of over 35's thought first time buyers should be able to draw on their pensions for a house deposit – with limits and guarantees.

66% believe that it is important to limit access to pension money to 55 plus.

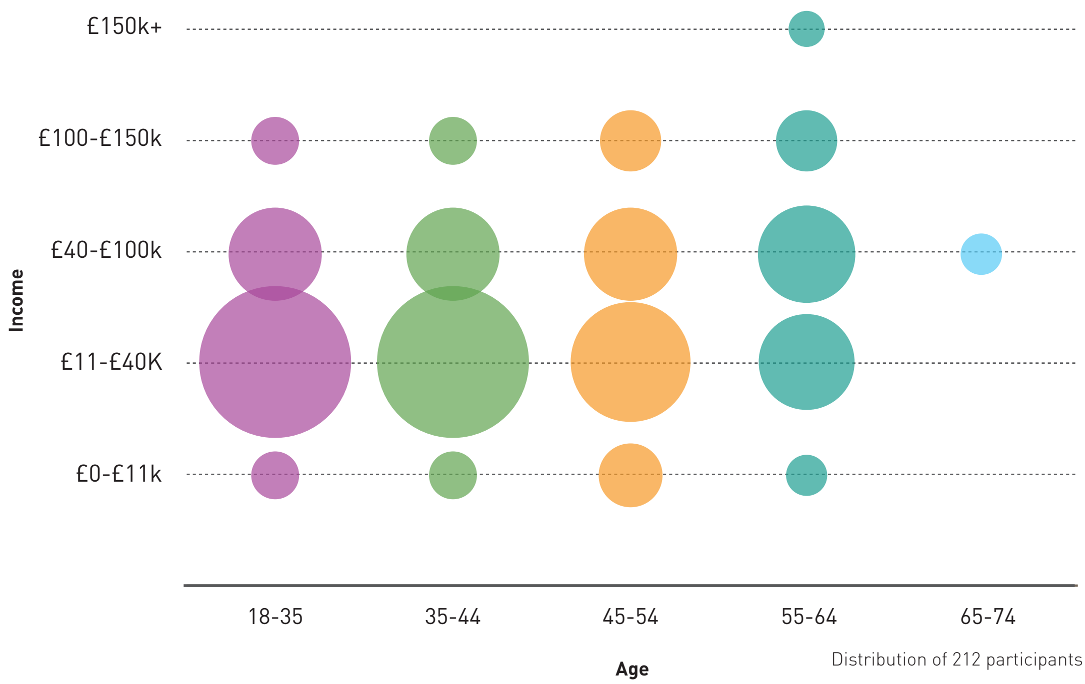
CONCLUDING THOUGHTS

- **People know they need to but find it hard to plan for their retirement**
- **Pensions are just not attractive as they are currently presented – old fashioned, complex, remote**
- **Scare stories of the pension gap do not motivate**
- **The current system of tax relief is not well understood and not a significant motivator**
- **Employee schemes are critical to get people saving earlier and more**
- **Simple, transparent matching contributions will motivate**
- **Greater accessibility, better communications and transparency are key.**

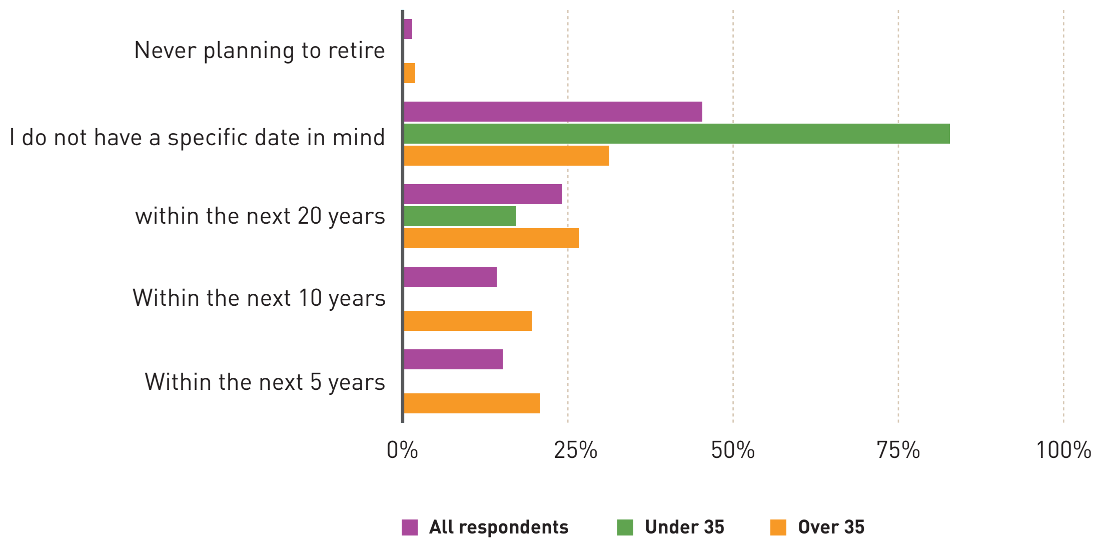
QUANTITATIVE RESEARCH

AGE AND INCOME PROFILE OF RESPONDENTS (Q1 & Q8)

Participants from a broad range of ages and income brackets



Q3 WHEN ARE YOU PLANNING TO RETIRE?



Retirement is a remote construct for working people.

It is normally seen and talked about as being a long way off... until suddenly it is just round the corner!

Q4 WHICH OF THESE MOST CLOSELY DESCRIBES WHAT RETIREMENT MEANS TO YOU?

Not working and spending time with friends and family (42%).

Spending my investments or pension and enjoying life to the full (33%).

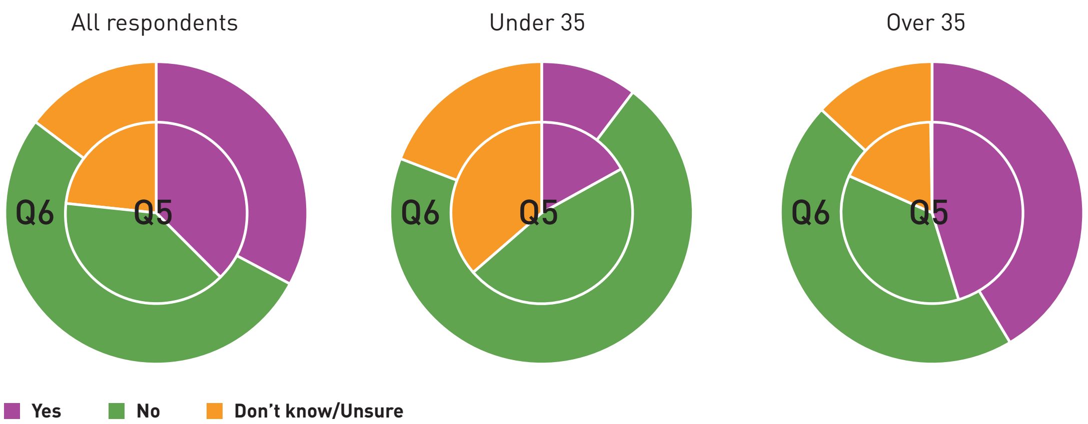
Working part time to top up my income (11%).

Working or volunteering with no or minimal pay because I enjoy it (11%).

I don't intend to retire (3%).

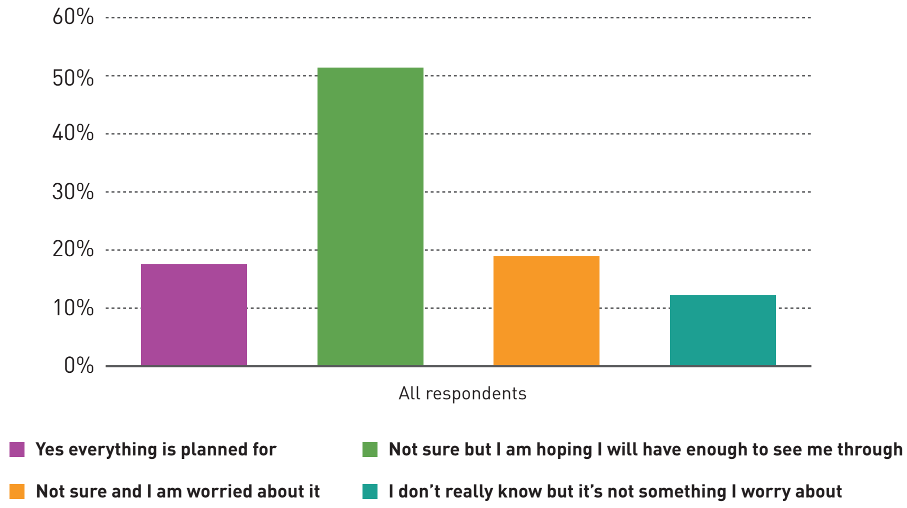
Q5 DO YOU KNOW WHAT SIZE PENSION POT YOU WILL NEED AT RETIREMENT TO FUND THE LIFESTYLE YOU WOULD LIKE?

Q6 DO YOU KNOW HOW MUCH YOU SHOULD BE SAVING EACH YEAR TO ACHIEVE THAT PENSION POT?



Most respondents do not know what size pension pot they need at retirement to fund the lifestyle they want. Even those that do know are unsure about how much to save to achieve it.

Q7 DO YOU BELIEVE YOU WILL HAVE ENOUGH MONEY TO RETIRE WHEN YOU PLAN TO FROM YOUR PENSION INCOME OR OTHER MONEY THAT YOU HAVE SET ASIDE?

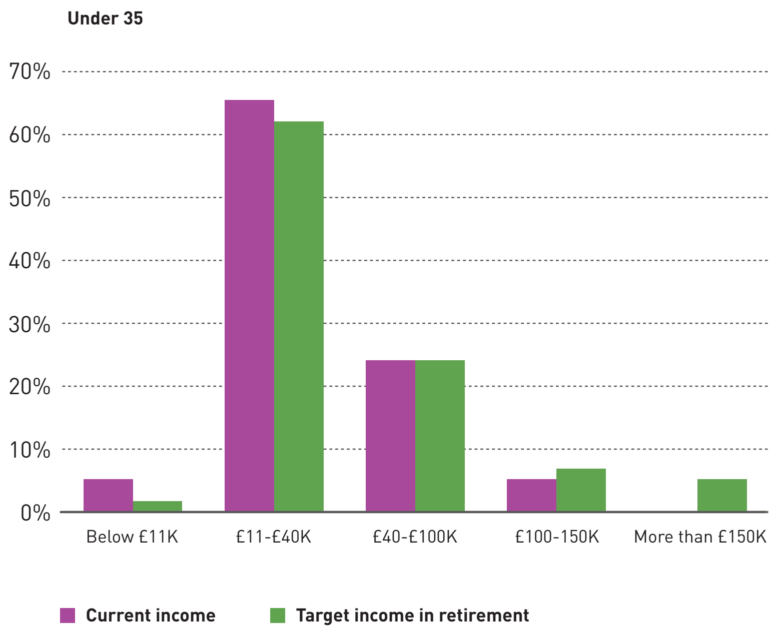


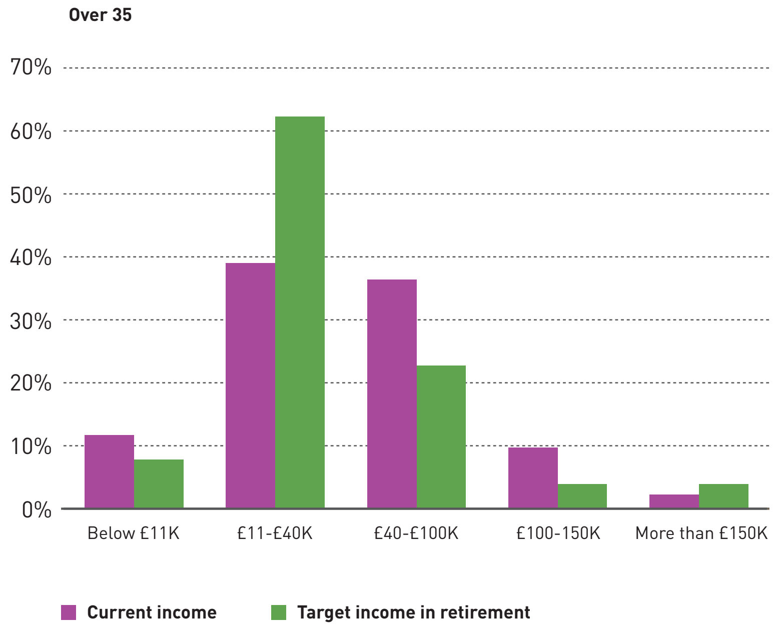
Only 18% of respondents appear to have planned appropriately for retirement.

The majority are hoping for the best!

Q8 WHAT IS YOUR CURRENT INCOME?

Q9 WHAT IS YOUR TARGET INCOME IN RETIREMENT?

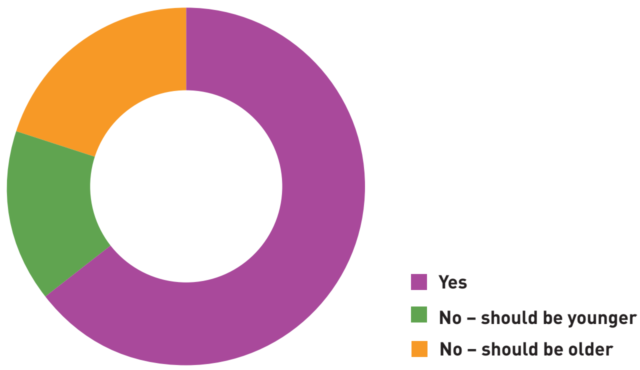




Overall there is an expectation, or hope to earn more in retirement than they currently earn.

High earning under 35's appear aspirational, mid earning over 35's appear more realistic.

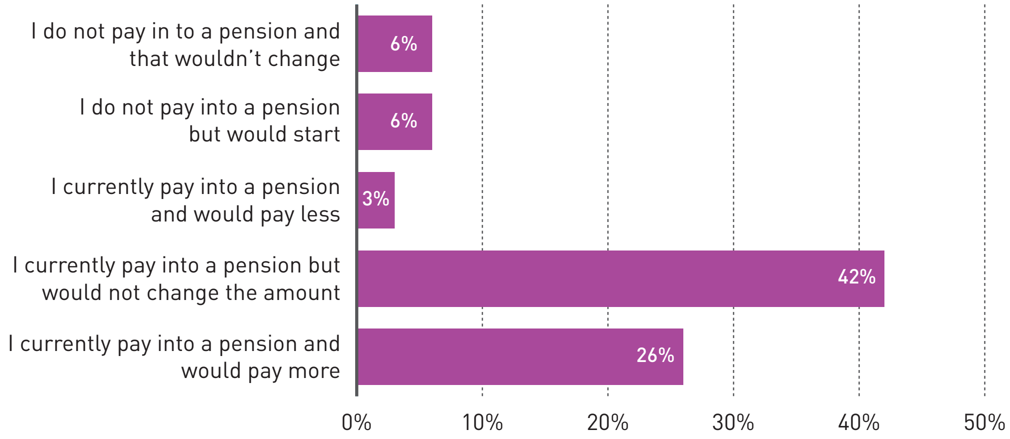
Q10 UNDER THE CURRENT PENSION RULES, YOU CANNOT ACCESS ANY OF YOUR PENSION FUND BEFORE YOU REACH AGE 55. DO YOU THINK THIS IS THE RIGHT AGE?



Q11 DO YOU THINK IT IS IMPORTANT TO HAVE A RULE THAT STOPS PEOPLE TAKING MONEY OUT OF THEIR PENSION BEFORE THEY REACH AGE 55?

Over 66% feel its important to stop people withdrawing from pensions until they reach the age of 55.

Q12 IF YOU WERE ALLOWED TO MAKE WITHDRAWALS BEFORE AGE 55, WOULD YOU PAY MORE OR LESS INTO YOUR PENSION PLAN?

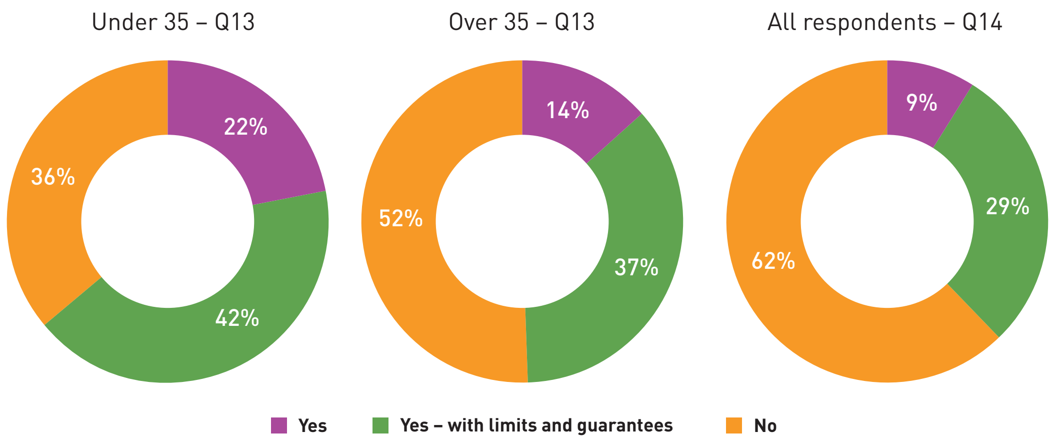


"Don't know" not charted

Allowing withdrawals could increase saving into pensions either by increased contribution or by starting a new pension, however over 40% say that it would not change the amount they save.

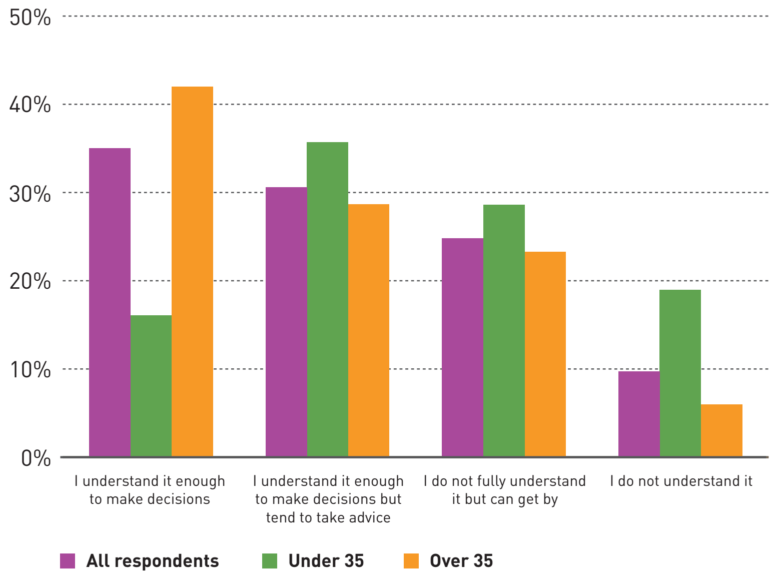
Q13 DO YOU THINK THAT FIRST TIME BUYERS SHOULD BE ALLOWED TO WITHDRAW THEIR PENSION SAVINGS TO USE FOR A DEPOSIT ON A HOUSE PURCHASE? (UNDER 35 – OVER 35)

Q14 DO YOU THINK THAT PEOPLE AGED UNDER 55 SHOULD BE ABLE TO WITHDRAW THEIR PENSION SAVINGS TO SUPPORT OLDER FAMILY MEMBERS? (ALL RESPONDENTS)



Younger respondents are keen to have some flexibility to be able to get on the property ladder. The majority do not want flexibility to be able to help older family members...

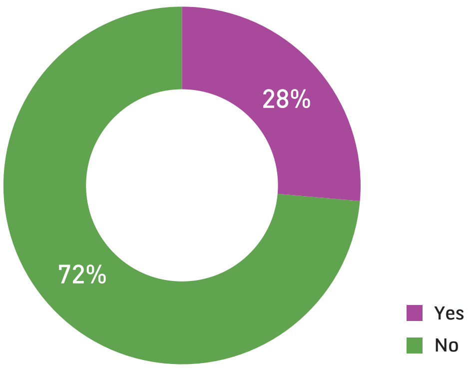
Q15 HOW MUCH DO YOU UNDERSTAND ABOUT THE CURRENT SYSTEM?



"This discussion shows just how baffling and clear as mud it is for the general person.".

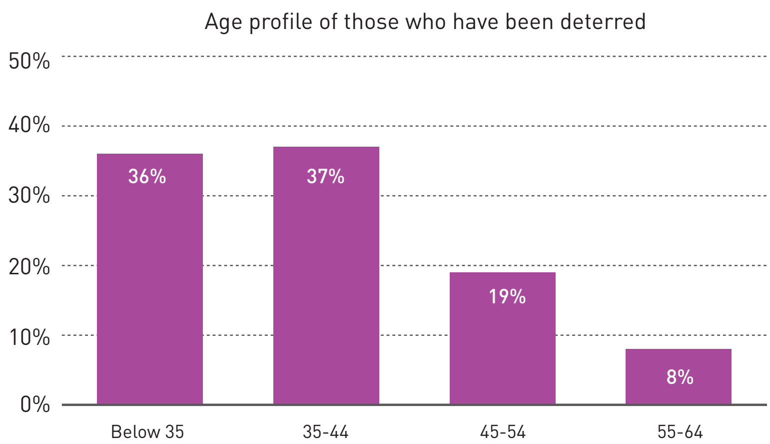
Focus Group Participant Female c50

Q16 DOES THE COMPLEXITY OF THE CURRENT SYSTEM DETER YOU FROM SAVING?

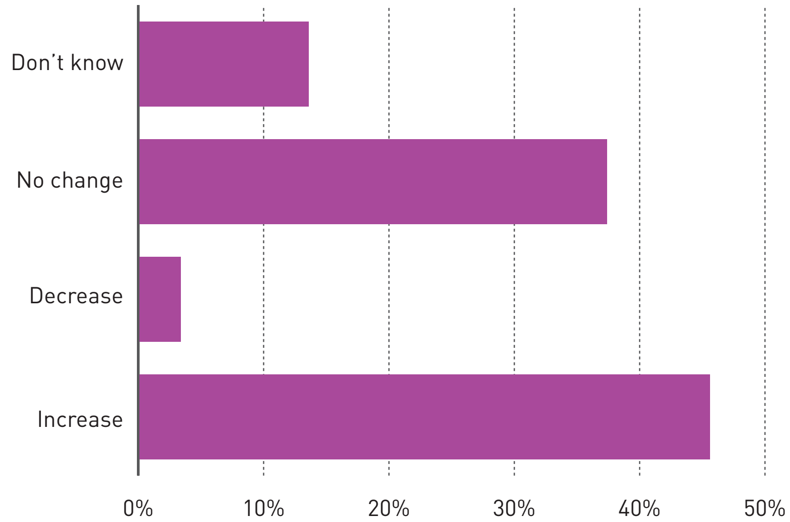


Complexity of the system is not a major deterrent to saving...

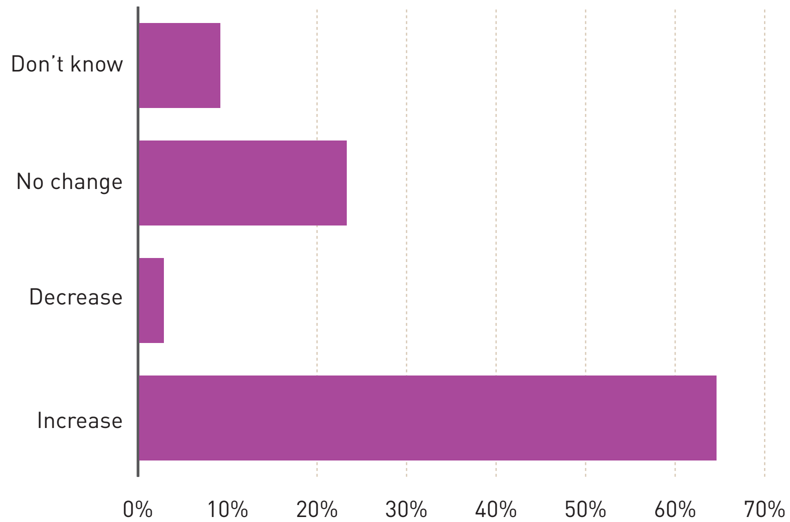
The closer respondents were to retirement, the less any complexity deterred them...



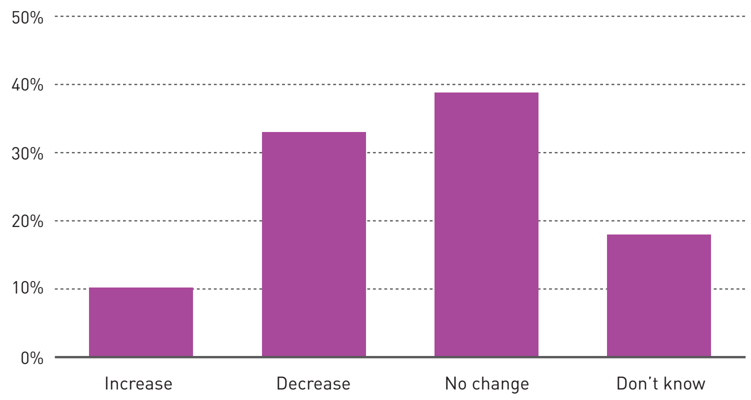
Q17 WOULD YOU INCREASE OR DECREASE YOUR PENSION CONTRIBUTIONS IF, INSTEAD OF THE CURRENT SYSTEM OF TAX RELIEF, THE GOVERNMENT MATCHED PENSION CONTRIBUTIONS WITH £1 FOR EVERY £3 YOU PUT IN?



Q18 WOULD YOU INCREASE OR DECREASE YOUR PENSION CONTRIBUTIONS IF, INSTEAD OF THE CURRENT SYSTEM OF TAX RELIEF THE GOVERNMENT MATCHED PENSION CONTRIBUTIONS AT A MORE GENEROUS RATE WITH £1 FOR EVERY £2 YOU PUT IN?



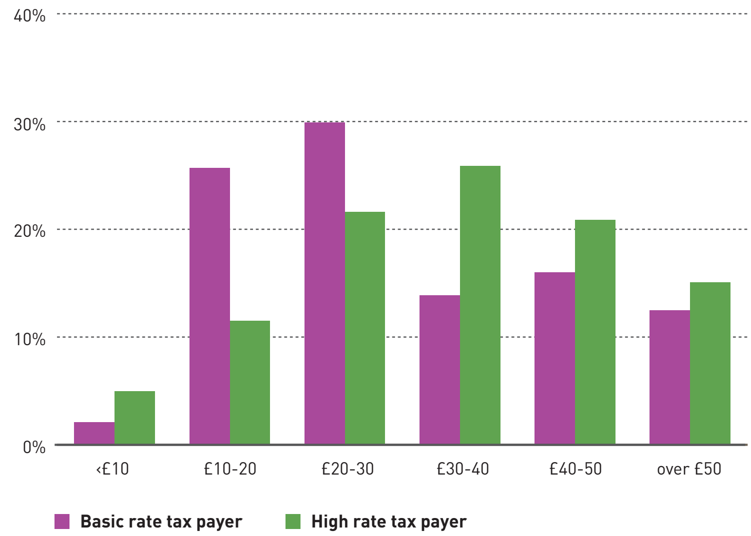
Q19 WOULD YOU INCREASE OR DECREASE YOUR PENSION CONTRIBUTIONS IF THERE WERE NO TAX RELIEF OR NO GOVERNMENT MATCHED CONTRIBUTIONS?



Removing the Government contributions to pensions would have an impact on contributions.

But not as big an impact as might be expected.

Q20 & Q21 WHAT IS THE MINIMUM LEVEL OF GOVERNMENT CONTRIBUTION THAT WOULD ENCOURAGE YOU TO SAVE INTO A PENSION – SO FOR EVERY £100 THAT YOU CONTRIBUTED, HOW MUCH WOULD YOU WANT THE GOVERNMENT TO CONTRIBUTE?



The current levels of Government contributions broadly match the expectations of both high and basic rate tax payers… or have the levels set the expectation?

Q22 THERE ARE TWO OPTIONS FOR HOW LONG TERM SAVINGS CAN BE INCENTIVISED. WHICH OF THESE OPTIONS DO YOU PREFER:

1. Pay tax on my earnings in the normal way and then choose to save into a pension or ISA and draw it out tax free when I need it

68%

However, our qualitative research clearly indicated that, when the options were explained further, people opted for the current system!

2. Pay no tax now but defer the tax and pay it when I draw the money from my pension

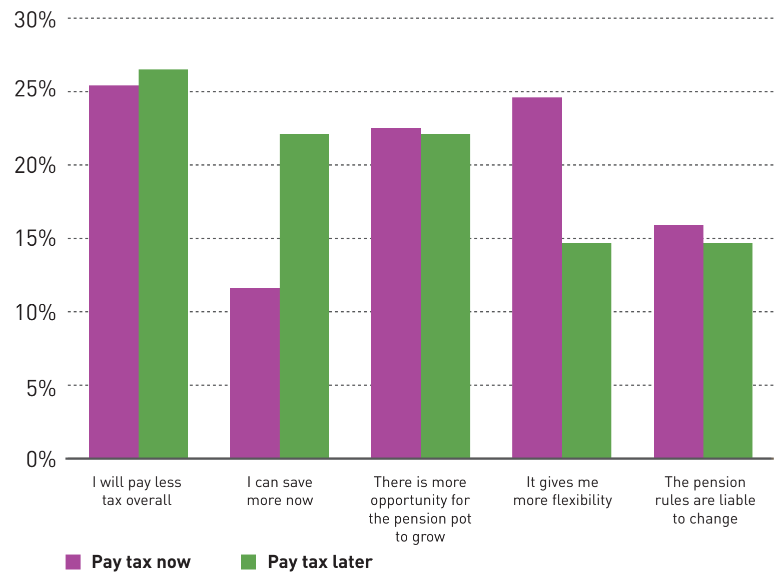
32%

"I don't look at the figures that are banded around as they will change by the time I'm retired...they could change in the next budget, the next autumn statement or even at the end of next week."

"In terms of incentives to save, I think not getting taxed at the point of earning is better."

"There's a better way of encouraging people to save than a complex tax system such as that."

Q23 WHICH OF THE FOLLOWING BEST DESCRIBES WHY YOU FAVOUR THE OPTION YOU SELECTED:



"I don't want to pay tax at a time when earnings will be lower."

"I want to pay tax now when I can afford it."

"The effect of compound interest, but also because this avoids having generations of older people paying no tax into the system in the future, almost inevitably leading to future Governments needing to change the legislation to compensate."

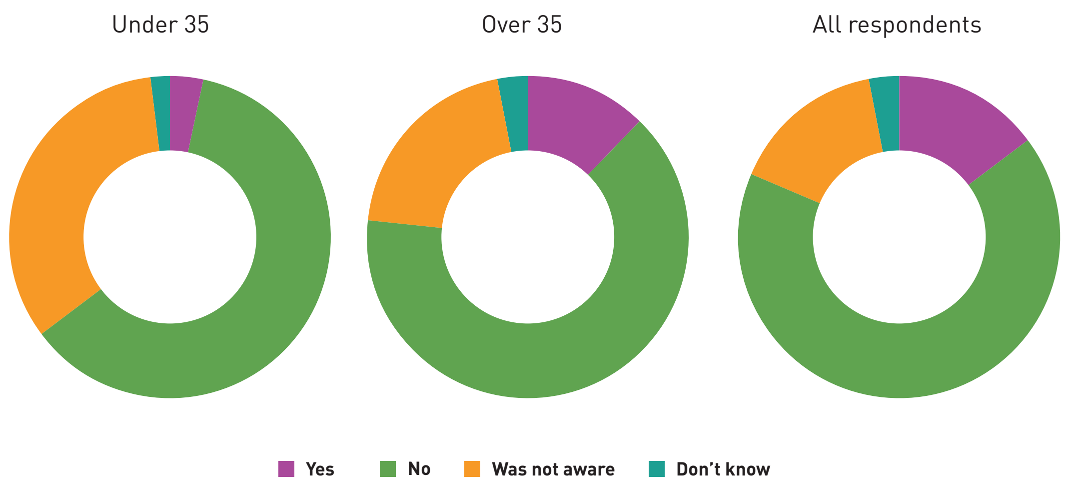
Q24 DO YOU THINK THERE SHOULD BE A LIFETIME LIMIT?

34% Yes

46% No

Although 46% were against a limit, this may be driven by it being seen as a "government limit" and not liking being told what they can do with their money...

Q25 DOES THE LIFETIME ALLOWANCE OF £1 MILLION DETER YOU FROM SAVING IN A PENSION?

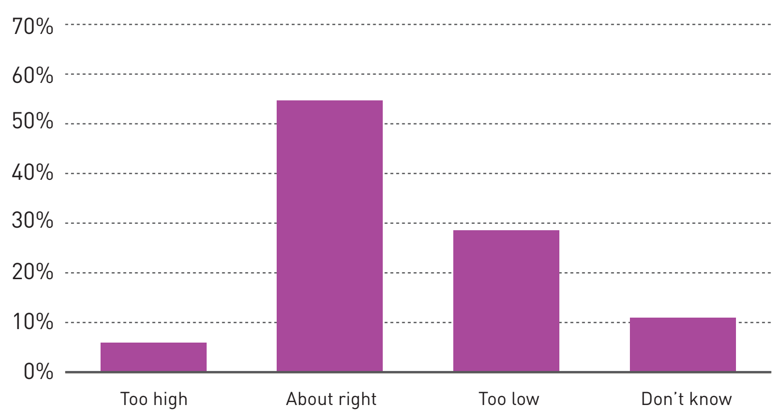


The cap of £1m is not a deterrent and 20% of people were not even aware of it.

The closer to retirement you are the more awareness and relevance it appears to have to respondents.

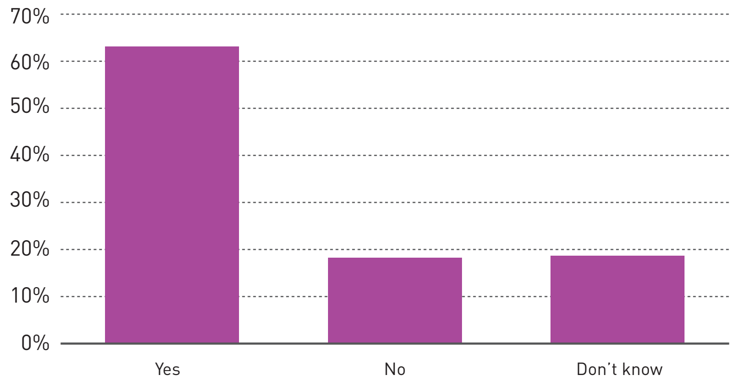
Q26 UNDER THE CURRENT PENSION SYSTEM YOU ONLY RECEIVE INCOME TAX RELIEF ON YOUR CONTRIBUTIONS AND ANY EMPLOYER CONTRIBUTIONS UP TO A TOTAL OF £40,000 FOR EACH TAX YEAR.

Do you feel that the £40,000 a year maximum for pension contributions is too high or too low?



Q27 CURRENTLY YOU CAN TAKE A TAX FREE CASH SUM FROM YOUR PENSION ON RETIREMENT OF ONE QUARTER OF YOUR PENSION POT. THERE IS A MAXIMUM TAX FREE CASH SUM OF £250,000.

Do you feel that this maximum figure of £250,000 is fair?

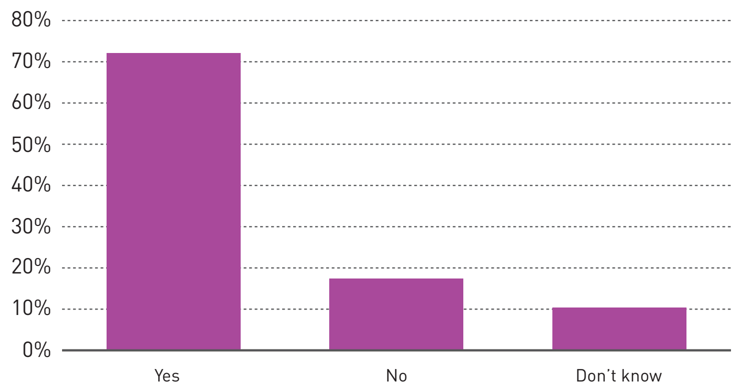


Q28: IF "NO" HOW MUCH DO YOU THINK IS FAIR?

- As much as you want
- £500,000
- All of it!
- All of your withdrawal, as after all it's likely you're going to sink it back into the economy and pay tax through that anyway
- Not sure
- Up to 50% tax free as this allows people to enjoy their hard earned pension more. Trades annual income for immediate cash
- 25% with no upper limit

Selected verbatim answers

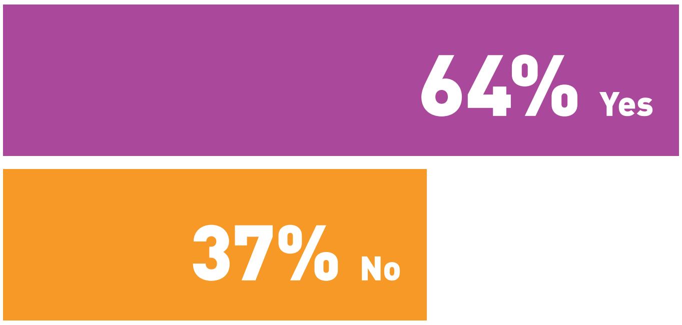
Q29 GIVEN THAT MOST PEOPLE DO NOT SAVE ENOUGH FOR THEIR PENSION, DO YOU THINK THAT THE GOVERNMENT SHOULD MAKE IT COMPULSORY TO SAVE IN TO A PENSION?



Respondents want compulsion, flexibility, limits on some aspects of pensions, freedom on others...

And this all varies by age, income and profession...

Q30 WOULD YOU BE PREPARED TO PAY IN 10% OF YOUR TAKE HOME PAY INTO YOUR PENSION IF YOUR EMPLOYER AND THE GOVERNMENT PUT IN ANOTHER 5%?



Q31 WOULD YOU BE PREPARED TO PAY IN 8% OF YOUR TAKE HOME PAY INTO YOUR PENSION IF OUR EMPLOYER AND THE GOVERNMENT PUT IN ANOTHER 7%

Q32 WHAT FACTORS MAKE IT DIFFICULT TO PUT ASIDE MONEY FOR YOUR PENSION? (TOP 2)

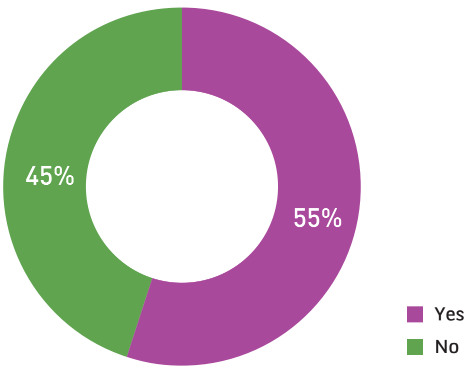
All respondents	Over 35	Under 35
Spent on non discretionary bills (mortgage/bills/etc)	Spent on non discretionary bills (mortgage/bills/etc)	Saving for a deposit on a property
Paying down debt	Paying for education for children or grandchildren	Spent on non discretionary bills (mortgage/bills/etc)

Q33 WHAT EXPENDITURE COULD YOU CUT BACK ON TO PUT MORE INTO A PENSION? (TOP 4)

Many respondents feel they could cut back on certain aspects of expenditure, however 25% state that they could cut back on "none of the above"...

Is saving into a pension a priority?

Q34 DO YOU THINK THAT FOR THOSE INDIVIDUALS WHO ARE SELF-EMPLOYED, THERE SHOULD BE DIFFERENT PENSION RULES THAT ALLOW FOR A MORE GENEROUS CONTRIBUTION FROM THE GOVERNMENT TO COMPENSATE FOR OTHER BENEFITS THEY DO NOT RECEIVE?



Although not a big majority, there is support for more generous contributions for the self employed...

Q35 PLEASE IDENTIFY ANY OTHER FACTORS WHICH YOU THINK WOULD ENCOURAGE YOU TO SAVE FOR YOUR RETIREMENT:

- Lower cost of living
- Clearer communications
- Tax incentives
- Reduce or remove tax on shares held within a pension
- Access
- Tax relief on school fees
- Consistency of government policy
- No deadlines on ISA's
- Lower fees on products
- Knowing how much to save to achieve a certain income in retirement
- Allow me to invest myself, funds are dreadful
- A pensions lottery – saving for pension buys you a ticket to a prize draw
- Tax relief for stay at home spouses
- Make it compulsory
- More straight forward information & communication
- Make it like a savings account

APPENDIX
QUALITATIVE RESEARCH - FOCUS GROUP QUOTES
QUANTITATIVE & QUALITATIVE SUMMARY

FOCUS GROUP QUOTES

“I think about it when I get paid every month because they take my pension contribution out of it.”

“Pensions are low down on my list of thoughts at the moment.”

“I would like the freedom to able to continue working if I wanted to, but have the financial flexibility for that not to be necessary.”

“I think now I’m paying school fees, but I can’t throw myself into a pension until I get past that milestone. And am hoping that I’ve done the best for them now for them to earn enough money.”

“I think we need to think about the trust we place on a pension provider as I wouldn’t be able to check whether they’re right or not, and there might be some horrible error in there!”

“Pension terms aren’t exactly everyday parlance.”

“[This discussion on pensions] shows just how baffling and clear as mud it is for the general person thinking about a comfortable retirement.”

“I don’t look at the figures that are bandied around as they will change by the time I’m retired… they could change in the next budget, the next autumn statement or even at the end of next week.”

“I certainly don’t think the Government should keep changing the rules and if I can stay invested during retirement then that’s a good thing. But if the rules keep changing… I have a financial background and I have an interest in finance up to a certain point but I already spend more of my life on this than I would care to… It’s just hard work.”

“There is an important difference between retirement and taking out your pension.”

“There should not be a scenario where when I reach retirement, whatever I saved which I though was enough is now not enough.”

“I would strongly associate retirement with enjoying myself and having time to do things which I can’t do now.”

“I wouldn’t think about saving for anything else before saving for a house deposit.”

“Definitely won’t retire at 65”“I know about the 25% free but after that I have a very vague understanding.”

“Maybe we don’t retire at 65, but at 75, and some people today are retiring later and later, so in our minds, it’s so far away that we’re not really that interested in it, we’re more interested in current things such as buying a house.”

“Once you get on the property ladder, your focus starts to shift to saving for the future.”

“Do I put my money in the hands of some unknown asset manager who might manage it well or not very well, or do I look after it myself and choose to do with it how I will today.”

“I wanted a private pension so I could have it under my control, basically just so I could have access to it rather than leave it dormant.”

“I want to manage my pension myself as I have my own investment horizon and my own views. So instead of paying a fee to a manager to run my money they way they see fit, I’d rather run it the way I see fit.”

"There's a better way of encouraging people to save than a complex tax system such as that."

"If I joined a firm and they didn't mention a pension at all then I probably wouldn't have noticed."

"At the start you don't think about the tax relief because it's not immediate."

"Out of sight, out of mind."

"The current system is fair, I think a flat rate is unfair on the higher earners."

"You're taxed at the marginal rate for a reason."

"Defeats the purpose of a pension."

"My secondary thing to channel money towards is my own investments rather than a pension pot."

"We don't want to put our cash away until we're 55, we want to be able to access it when we need it" Male.

"We're not going to only rely on our pensions. We're going to have our savings to prepare us, our property portfolios" Male c30 "making our own life portfolio."

"In terms of incentives to save, I think not getting taxed at the point of earning is better."

"I think yes [you should get a self-employed pension], because there are a lot of benefits you get from being part of a big company including a pension, that self-employed people just don't get."

"If you're the government and you're trying to encourage people to save, it should be a fairly even system whether you're self-employed or employed right?"

"If you were better shown that what you were putting away today will give you tomorrow… it might be more incentive" Male c25 "It's not your pension until the day you get it."

"It would incentivise you more to save [if you felt more ownership of it]."

"If it's through tax relief, no, if it's an explicit contribution at the same time as your employer did it then yes."

"It seems so far away, the money isn't yours at the minute."

TISA
Dakota House
25 Falcon Court
Preston Farm Business Park
Stockton-On-Tees
TS18 3TX

Technical queries: 01642 666999
Administration: 01642 666982

enquiries@tisa.uk.com
www.tisa.uk.com

Tax Incentivised Savings Association Limited. A Company Limited by Guarantee. Registered in England and Wales No. 3548792

Designed and printed by studio401