Public Bill Committee

TAXATION OF PENSIONS BILL

WRITTEN EVIDENCE

PUBLISHED BY AUTHORITY OF THE HOUSE OF COMMONS
LONDON—THE STATIONERY OFFICE LIMITED

PBC (Bill 097) 2014–2015
Contents

Low Incomes Tax Reform Group (TP 01)
Association of Consulting Actuaries (ACA) (TP 02)
Ros Altmann (TP 03)
Stephen Ward (TP 04)
Mark Hattersley (TP 05)
Towers Watson's (TP 06)
Just Retirement (TP 07)
Friends Life (TP 08)
Talbot and Muir (TP 09)
John Greenwood (TP 10)
Hargreaves Lansdown (TP 11)
Association of Taxation Technicians (ATT) (TP 12)
ABI (TP 13)
National Association of Pension Funds (TP 14)
National Association of Pension Funds—supplementary (TP 15)
Financial Conduct Authority (TP 16)
Brittania Financial Services Ltd, Auckland, New Zealand (TP 17)
Partnership Assurance Group plc (Partnership) (TP 18)
Written evidence

Written evidence submitted by the Low Incomes Tax Reform Group (LITRG) (TP 01)

PRACTICAL ISSUES ARISING FROM NEW PENSIONS LEGISLATION

1. Our comments below are not in relation to policy: that is something that is decided by politicians. Instead, we concentrate on areas where, unless proper procedures are put in place, many taxpayers may find themselves with large tax bills to pay unexpectedly or alternatively having to reclaim significant amounts of tax.

2. ABOUT US

2.1 The Low Incomes Tax Reform Group (LITRG) is an initiative of the Chartered Institute of Taxation (CIOT) to give a voice to the unrepresented. Since 1998 LITRG has been working to improve the policy and processes of the tax, tax credits and associated welfare systems for the benefit of those on low incomes. Everything we do is aimed at improving the tax and benefits experience of low income workers, pensioners, migrants, students, disabled people and carers.

2.2 LITRG works extensively with HM Revenue & Customs (HMRC) and other government departments, commenting on proposals and putting forward our own ideas for improving the system. Too often the tax and related welfare laws and administrative systems are not designed with the low-income user in mind and this often makes life difficult for those we try to help.

2.3 The CIOT is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT’s primary purpose is to promote education and study of the administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it—taxpayers, advisers and the authorities.

3. EXECUTIVE SUMMARY

3.1 The current PAYE system is ill-equipped to deal with the new pensions regime and this could result in thousands more interactions with HM Revenue & Customs (HMRC) by taxpayers.

3.2 For those taxpayers who end up with a tax underpayment as a result of accessing pension funds, some may have no funds left with which to pay the additional tax due.

3.3 For those taxpayers who end up due a tax refund as a result of accessing pension funds, it is not clear how quickly those refunds may be accessed.

3.4 Increased contacts to HMRC as a result of the points above may cause severe difficulties for contact centres at peak times.

3.5 Low income taxpayers may withdraw funds without understanding the effect it might have on their state benefits.

3.6 Clear guidance is essential for all those who are considering accessing their pensions savings. This is a very complex subject and their pension fund may represent one of the largest assets in an individual’s hands. Skimping on guidance and communication at implementation is likely to lead to unforeseen tax charges, unhappy pensioners and an overworked HMRC.

3.7 We recommend a 14-day cooling off period once a request for pension payment is made so that the taxpayer may be provided with full information as to the taxation consequences.

4. BACKGROUND TO THE CURRENT PAY AS YOU EARN (PAYE) SYSTEM

4.1 The PAYE system operates by instructing the payer (normally an employer or pension provider) to deduct income tax (and National Insurance contributions (NIC) for an employee) from employees’ pay on a cumulative basis over a tax year. A code number is issued to the employer or pension provider that enables them to make sure that the allowances allocated to that employee for that employment are evened out over the tax year; in some cases the employer will simply be instructed to deduct a standard rate of taxation. This latter case is often the position for a second employment or for a small pension, where all of an individual’s tax free allowances are allocated to the first employment: the second employer would then deduct tax at the rate it was instructed. An issue arises because if the second employer is instructed to deduct tax at basic rate, say, but part or all of the income should have been taxed at higher rates, further tax will become due. Similarly, if the first employment does not use all of the individual’s allowances, the individual may be due a refund at the year end (depending on their other income).

5. TAX DEDUCTIONS FROM PENSIONS WITHDRAWAL

5.1 Under the “new” regime, taxpayers will be subject to income tax on amounts they receive from their accumulated pension pots, subject to 25% being tax-free. This section questions how the tax that is due (on the 75% that is taxable) is to be collected.
5.2 This new regime is intended to be flexible so that a taxpayer may withdraw more in one year than in the following year or indeed nothing in one year, and so on. A taxpayer may well have a number of pension pots and choose to access more than one at a time—or to access some in one year and some in other years.

5.3 In the simplest case a taxpayer would have no other income in the year. Accordingly he could set his personal allowance against the “pension income” (in other words the 75% of his withdrawal that is taxable). But how will the tax due on the pension income be collected? Given the number of people involved it seems likely that some deduction at source will have to be made by the pension provider. The pension payer will not have to report any payments separately to HMRC as “this information is expected to be available to HMRC through Real Time Information”. Will a pension payer be allocated a tax code? Or will a straightforward basic rate tax deduction be made from such payments? If we assume that a tax code will be issued to a pension payer:

a. Will that code include the taxpayer’s personal allowance, or will it automatically enforce a tax deduction at the basic rate?

b. Given that many taxpayers may access more than one “pension pot”, how will HMRC allocate personal allowances and/or tax rates between them?

c. HMRC intend to withhold certain Notices of Coding where a change in coding would have no effect on the taxpayer. If a taxpayer has multiple sources of income, and does not have access to all Notices of Coding, they may not be able to “piece together” how all of their allowances are being used (see also 5 below).

d. Future plans to open up the PAYE system for employees and pensioners to view and make changes online and immediately may help (or hinder?) but this will not help those who are digitally excluded or simply have no understanding of the coding system (or perhaps even the tax system as a whole) even if they can operate a computer.

5.4 If we assume that basic rate tax will be deducted by the pension payer:

a. Many taxpayers may suffer deductions that are inadequate if deductions are only at the basic rate. Will the pension payers be required to draw this possibility to the attention of the taxpayer? (See our comment above about a possible cooling off period.) Will HMRC draw this to the attention of the taxpayer, for example, by a note on the code number issued? For individuals who have now left employment and who might be tempted to spend this sum (for example, on repaying a mortgage), they may have little cash in the future to pay any outstanding tax bill.

b. On the other hand, many low income taxpayers might find that a basic rate deduction from their pension income would mean they had suffered excessive tax. Such low income taxpayers are also the ones who might most need their tax refund early. Currently most such taxpayers require to wait until after the end of the tax year to obtain a tax refund. Once their total income is known, then HMRC issue tax refunds. This could result in a delay of over a year before the tax was refunded (see section 4 below for further comments).

5.5 Having “sold” the new pensions legislation as providing easier access to pensions savings, taxpayers will assume that their pension companies will be able to make payments to them quickly so the tax system needs to accommodate this and mirror the speed and ease elements too.

6. END OF YEAR TAX PROCEDURES FOR PENSIONERS

6.1 Many pensioners will have had little to do with HMRC up until retirement, their tax affairs having been dealt with via PAYE. These pensioners will not be in the habit of completing a self assessment (SA) tax return—a long and complex document. Instead it is likely that HMRC will have reconciled their tax liability each year outside the SA system by issuing a form P800. To date many people will have had small adjustments at the year end, resulting in small refunds or small underpayments that were collected via PAYE in a subsequent year, thus requiring no physical payment by them.

6.2 Given the many combinations of withdrawals from pension pots that pensioners might make in a year (and possibly in multiple years), almost inevitably more significant underpayments and overpayments of tax will accrue to these pensioners. We do not know how this will be administered by HMRC. Will they insist on SA tax returns being completed or will they rely on the P800 system? Consistent guidance is needed so that the expectations of pensioners can be managed.

6.3 Suddenly finding themselves in a position where they are due to pay additional tax may be bewildering and upsetting. How will any such tax be collected? Will they be given the opportunity to pay it over a period of time or will it be collected in one lump sum? Understanding the answers to these questions is crucial for pensioners. Unless they understand when any further tax bill may fall due (and the extent of that bill) some may find themselves in a spiral of having to unlock further funds from pension pots in order to pay past tax liabilities—thus generating a further tax bill. If any demand is issued via a P800, there is still the possibility of having to place the taxpayer in self assessment in order to collect the liability (if the taxpayer does not pay when asked to pay “voluntarily”) and with that will come its own challenges, especially the rigid penalty regime if a pensioner misses a deadline or cannot file online:

19 HMRC draft guidance on the Pensions Bill, Chapter 8.
For those pensioners who were previously in SA, how will the system identify those taxpayers who no longer require to be in SA and so remove them from SA as soon as possible?

What guidance will be offered around all this in a clear and easy to access format, remembering that many pensioners are digitally excluded?

7. **IN-YEAR TAX REPAYMENTS**

7.1 As noted above, some pensioners may find that the tax deducted from their pension income is excessive. A mechanism needs to be available to allow early repayment of that tax, particularly to the less well-off.

7.2 Alternatively, for low income pensioners where it is clear that a basic rate tax deduction would be excessive, will HMRC introduce a system where the pension could “self-certify” that no tax would be due and so receive the payment gross (without tax deduction)? Such a scheme operates now for receiving bank interest without tax being deducted (using form R85).

8. **INTERACTION WITH STATE PENSION**

8.1 Already pensioners often find themselves in an underpayment situation following receipt of the state pension as it is often not coded in properly when it is first received. Taking either a lump sum or additional income might push individuals into paying tax at higher rates.

8.2 Someone who previously had one source of employment income may find themselves receiving a state pension (that is not taxed at source, but the tax on which is collected via a Notice of Coding used by an employer or pension payer), a works pension of a regular amount and various ad hoc amounts from private pension schemes. If pensioners are issued with more than one Notice of Coding, will they understand the need to check them together? We understand a unified notice of coding is being developed but in the meantime much clearer guidance will need to be provided to this group.

9. **INTERACTION WITH STATE BENEFITS**

9.1 Accessing a lump sum or pensions income might push some pensioners over the thresholds at which certain state benefits are paid. This is a serious issue for the lower paid, who might unwittingly both face an unexpected tax bill, but also find that they are being denied state benefits to which they would otherwise have been entitled. Clear guidance is needed for these individuals.

10. **INTERACTION BETWEEN HMRC AND DWP**

10.1 Because of the interactions noted above, data flow between HMRC and Department for Work and Pensions (DWP) must be such that a pensioner can rely on them cooperating and producing the correct tax codes. Should their systems fail so that a pensioner is left with an unexpected underpayment, there needs to be a clear and fair method of dealing with these underpayments (including writing them off, where necessary).

11. **PENSIONERS MOVING OVERSEAS**

11.1 Increasingly pensioners move overseas. Specific protocols are needed to deal with their change of circumstances, with clear guidance and support.

12. **PENSIONERS AND SAVINGS**

12.1 With their lump sums and/or balance of their pension pots, many pensioners may choose to keep a nest-egg in a bank. For many of these a 0% tax rate may be applicable. How is this to be administered and publicised? How will they be made aware that taking a further tranche of pension income may cost them some or all of their 0% tax rate entitlement?

13. **SOME SCENARIOS TO ILLUSTRATE THE ABOVE POINTS**

13.1 Wilfred and Wilhemina, late 50s. He continues in employment. She, no longer working, decides to prop up the household income by starting to draw on her smallish pensions. She reckons she can afford to withdraw £5,000 a year until her State pension kicks in. She takes two payments a year. Clearly with no actual tax liability (because her personal relief covers the pension withdrawals), must she suffer a basic rate tax (20%) deduction and reclaim each year? Can she self-certify as non-taxpayer and receive it gross? Must HMRC issue code(s) to pension provider(s)? What happens if in-year she suddenly takes out another £15,000 to pay off the mortgage?

13.2 Ernest and Brunhilde, mid-sixties, are within striking distance of receiving state pensions. He retires and starts receiving a final salary works pension, six months later claims the state retirement pension and thereafter starts drawing smallish sums from his collection of old defined contribution pension schemes in irregular amounts and at odd intervals to fund their holidays. What system will HMRC set up to collect the right amount of tax from his haphazard income? Will they tip him into the SA regime? Will they then leave him there even when he takes a couple of years off from raiding his pots? Brunhilde then claims her small state retirement pension of £5,500 a year and decides to cash in her two pots totalling £14,000 (of which 25% would be tax free, leaving £10,500 liable to taxation). How will the two different pension providers tax (or not) the
taxable £10,500? Will DWP and HMRC have cooperated in time so that her state retirement pension is also taken into account when establishing any tax deduction from her lump sum?

13.3 Ron has amassed sizeable pension pots close to £1 million, enabling him to drawdown a steady £40,000 a year without crossing the border into the 40% band. Deciding to build an extension, he extracts a lump sum of £150,000 in one year. How does the provider/HMRC sort out his sudden lurch into the loss of all personal allowances and the next two tax bands?

13.4 Ethel, 64, disabled and living on a small state pension, pension credit and an assortment of benefits, decides to take a trivial commutation of £25,000 from her old works pension. Who will 1) warn her of the possible impact on her benefits including any passported ones, and 2) advise DWP of her new circumstances?

November 2014

Written evidence submitted by Association of Consulting Actuaries (TP 02)

INTRODUCTION AND EXECUTIVE SUMMARY

1. The Association of Consulting Actuaries (ACA) welcomes the changes brought about by the Taxation of Pensions Bill 2014/15 and in particular the freedom of members to access savings in a manner that best suits their circumstances.

2. We believe the reforms will particularly benefit those with moderate pension pots and will help encourage individuals to save more.

3. In order to avoid abuse of the new flexibilities, we understand that the Government had to introduce measures to ensure that these new freedoms will not be abused. However, these measures add to an already overly complex regime. The regime is becoming so complex that most members of public will struggle to comprehend these complexities and may make inappropriate decisions as a result. We would prefer some genuine simplification of the pension tax regime but at the very least there should be clear information from HMRC in a form that the man in the street can access and understand. We hope that appropriate resources will be dedicated to producing this.

4. The ACA's 1,750 members provide advice to thousands of sponsors of UK pension schemes, including most of the country's largest schemes. ACA members are also scheme actuaries to schemes covering the majority of members of private sector defined benefit pension schemes. Increasingly, actuaries are involved in advising on defined contribution schemes and in providing advice to individuals on their pension planning and arrangements.

RATIONALE FOR MORE FLEXIBILITY

5. Prior to the budget announcement only those individuals with either very small pension pots or those with significant pension pots (such that they could secure a minimum pension income of £20,000pa) had flexibility around their pension pot. Although in theory individuals had the right to put their pension pots into drawdown, the regulatory burden around drawdown meant that few individuals could reasonably take advantage of this at a reasonable cost. The primary logic of the minimum income of £20,000pa was to ensure that individuals did not use all their retirement savings quickly and then become a burden on the state.

6. The introduction of the new single tier pension from April 2016 means that most individuals will be lifted out of means tested benefits and the requirement to prove a minimum income of £20,000 is therefore redundant.

7. As such, there seems no reason not to extend the same flexibilities to those with moderate size pots. However, there are other reasons why we believe this flexibility is appropriate.

8. The income needs of individuals in retirement are now more diverse:
   — Individuals change jobs more frequently.
   — There has been an increase in the proportion of women in employment and a reduction in men in employment.
   — Part time work is now far more prevalent.
   — People are less likely to reach retirement married to the same partner that they were married to in their twenties.
   — Both partners in a relationship might have worked and built up pensions in their own right.

9. As such, the traditional design of a pension scheme that provides the main income to the primary earner and protection benefits at half or two thirds that level for a spouse and beneficiaries is less relevant to today’s workforce.

BENEFITS TO THOSE ON MODERATE PENSIONS

10. Currently, the average Defined Contribution pot at retirement is below £30,000. At this level, following tax law changes in March it may be possible to cash out such funds as “trivial”. But if £30,000 is the average,
very many will have pots of no more than £50,000. When converted to an annuity this might provide an individual with an income of less than £30 per week before tax.

11. For an individual who has perhaps been involved in manual work for most of their working lives, it might be a significant struggle to carry on working through to a State Retirement Age of 67 and with the ability only to be able to secure a modest additional weekly income there is no possibility of being able to retire prior to then. However, the flexibilities introduced into the budget mean that such an individual might be able to consider part time work or earlier retirement. For example, an individual with a pension pot of £50,000 might be able to contemplate retiring at 64, drawing on their pension pot up to State Retirement Age and then relying on State benefits thereafter or part time work over a longer period.

12. Being able to access retirement funds in this way means that individuals will more readily see the benefit of saving for retirement, particularly at a time when annuities are seen as poor value for money and inflexible.

ENCOURAGEMENT FOR INDIVIDUALS TO SAVE MORE

13. As such, the flexibilities tackle the most significant issue that individuals are not saving enough for retirement. We see this as a much more significant issue than the form that retirement benefits take.

14. Much of the debate around whether to annuitise or not ignores the point that individuals have not saved enough for retirement. As such, individuals are often faced with the unpalatable choice that they either annuitise, in which case the reality of not saving enough for retirement is made all too clear by a substantive drop in income and hence lifestyle; the alternative, which is to reduce the lifestyle to a modest degree, recognising that this may be for a limited period, and then rely on state benefits after that period is often the preferred choice, whether consciously or subconsciously. Individuals can rationalise this on the basis that they will have the most income in the period of retirement when they are likely to be most active.

15. Furthermore, the initial experience by those in the pensions industry is that the changes have created greater interest in pensions and consideration of saving more for retirement.

CHALLENGES WITH THE NEW FREEDOMS

16. We recognise that, in hindsight, some members may not make the best decision and spend more of their retirement savings than is sensible. It is clear from the success of the various pension liberation scams that there is an intrinsic demand for more flexibility. By creating that flexibility (available to all from, usually, age 55) but with the support of guidance, we would hope that the scams can be minimised. However, it is not just guidance that will be key but also the complexity of the regime.

17. In order to avoid abuse of the new flexibilities, we understand that the Government had to introduce measures to ensure that these new freedoms will not be abused. However, these measures add to an already overly complex regime. The regime is becoming so complex that most members of public will struggle to comprehend these complexities and may make inappropriate decisions as a result. We would prefer some genuine simplification of the pension tax regime but at the very least there should be clear information from HMRC in a form that the man in the street can access and understand. We hope that appropriate resources will be dedicated to producing this.

FLEXIBILITIES FOR DEFINED BENEFIT SCHEMES

18. For defined benefit schemes, we see that there is merit in allowing members to transfer from defined benefit arrangements to defined contribution arrangements to take advantage of the same flexibilities. We recognise however, that in the majority of circumstances that a transfer from a defined benefit scheme might mean the loss of valuable certainty and we think it right that there is a requirement for financial advice. In due course, we think it would be appropriate for similar flexibilities with appropriate advice requirements to be capable of being offered directly from defined benefit schemes and thereby avoiding some transaction costs for the member.

19. We would be happy to clarify or explain these points in more detail and would be happy to provide oral evidence to the Committee.

November 2014

APPENDIX

SURVEY FINDINGS IN RESPECT OF THE ‘FREEDOM AND CHOICE’ REFORMS FROM THE 2014 ACA SMALLER FIRMS SURVEY

20. During the summer of 2014 the ACA conducted a survey of smaller firms’ (those with 249 or fewer employees) pension trends where defined contribution arrangements are prevalent, where any pension arrangements presently exist at all. The survey attracted 414 responses and included a number of questions and responses in respect of the ‘freedom and choice’ reforms now encapsulated within the Taxation of Pensions Bill.

20 See 2014 ACA Smaller Firms’ Pensions Survey Preliminary Report (www.aca.org.uk—publications page)
21. The survey found close to six out of ten of these smaller employers are supportive of the new freedoms spelt out in the reforms, with just one in ten opposed (see Figure 1). An even higher number, two-thirds, support in particular the removal of the remaining requirements for individuals to buy an annuity.

Figure 1
ARE EMPLOYERS GENERALLY SUPPORTIVE OF THE NEW ‘FREEDOM AND CHOICE’ REFORMS?

<table>
<thead>
<tr>
<th></th>
<th>1-9 employees</th>
<th>10-49 employees</th>
<th>50-149 employees</th>
<th>150-249 employees</th>
<th>All employers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Very supportive</td>
<td>21%</td>
<td>21%</td>
<td>15%</td>
<td>13%</td>
<td>18%</td>
</tr>
<tr>
<td>Supportive</td>
<td>35%</td>
<td>38%</td>
<td>41%</td>
<td>48%</td>
<td>40%</td>
</tr>
<tr>
<td>Neutral</td>
<td>10%</td>
<td>12%</td>
<td>8%</td>
<td>9%</td>
<td>10%</td>
</tr>
<tr>
<td>Not supportive</td>
<td>6%</td>
<td>5%</td>
<td>13%</td>
<td>22%</td>
<td>11%</td>
</tr>
<tr>
<td>Don’t know</td>
<td>28%</td>
<td>24%</td>
<td>23%</td>
<td>8%</td>
<td>21%</td>
</tr>
</tbody>
</table>

22. There is however less enthusiasm for the Government’s proposal that access to pension savings should move from age 55 to age 57 in 2028 (when the SPA moves up to age 67 with adjustments to the age thereafter keeping a 10-year gap between the two ages). Just 40% are supportive of this change with 32% opposed.

23. At the time of writing, the Government has not finalised its proposals on how the ‘guidance guarantee’ for those approaching retirement should work. The service proposed by the Chancellor aims to give those approaching retirement access to information to help them make an informed decision about how they should use their pension savings. As a result, it is unsurprising that across all sizes of employers, there is no clear view of the channels employees will use in seeking guidance. Where employers have taken a view, ‘face-to-face’ meetings are seen as likely to be the most popular channel, followed by web-based tools and then telephone guidance (see Figure 2).

Figure 2
EMPLOYERS’ VIEWS ON THE GUIDANCE CHANNELS THAT EMPLOYEES APPROACHING RETIREMENT ARE MOST LIKELY TO USE (IN RANKED ORDER)

<table>
<thead>
<tr>
<th>Ranking—1st ‘most likely’</th>
<th>1-9 employees</th>
<th>10-49 employees</th>
<th>50-149 employees</th>
<th>150-249 employees</th>
<th>All employers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Telephone guidance</td>
<td>4</td>
<td>4</td>
<td>5</td>
<td>4</td>
<td>4</td>
</tr>
<tr>
<td>Web-based tools</td>
<td>3</td>
<td>2</td>
<td>3</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td>Face-to-face meetings</td>
<td>2</td>
<td>3</td>
<td>2</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>Won’t use guidance</td>
<td>5</td>
<td>5</td>
<td>4</td>
<td>5</td>
<td>5</td>
</tr>
<tr>
<td>Don’t know</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
</tr>
</tbody>
</table>

Written evidence submitted by Dr. Ros Altmann, CBE (TP 03)

THIS RESPONSE IS SENT IN A PERSONAL CAPACITY, AS AN INDEPENDENT PENSIONS EXPERT

SUMMARY:
— Some of this Bill’s proposals are in danger of losing sight of practicality and customer needs.
— Requirements for those who access their pensions flexibly to notify all their other pension providers within 31 days and fines for failure to do so are unfair and unworkable in practice.
— These requirements are out of proportion to any likely tax leakage, indeed the ability to retain a £40,000 MPAA after cashing in up to three small pots of up to £10,000 each is likely to lead to far more tax loss than those failing to notify past providers about flexible access.
— Such requirements will disproportionately disadvantage the least well-off, who are least likely to have £10,000 a year to contribute to new pensions after flexible access and may not find time to trace old pensions until they are well into retirement.
— Wealthier individuals are more likely to have a financial adviser to help sort out their financial affairs and notify all old providers, whereas the average customer will struggle to find out who to write to, especially if still working and having little spare time.
AftEr flExiblE AccEss so thEy undErstAnd whAt is bEing sAid.

2. AdministrAtors should bE rEquirEd to usE A stAndArd form to notify customErs About thE lowEr mPAA

And unworkAblE

1. r EquirEmEnts for customErs using flExiblE AccEss to notify All thEir othEr PEnsion ProvidErs ArE unfAIR
company, rather than allowing each one to report in their own way. The form should explain the situation in

— I suggest relying on people to obey the rules, as happens now in flexible drawdown, then penalising
— Alternatively, require those who have used flexible access only to notify new pension providers, or
— I have concerns about communications sent by providers to customers, informing them about the
  lower Money Purchase Annual Allowance following flexible access. A standard form and wording
  is required, so individuals can understand what they are being told. There is too much risk of
  impenetrable jargon leading customers to inadvertently break the rules.
— There should be standardised official forms for pension statements for those reaching pension age.
  A simple one page summary of their pension account balance, type of fund and any special features,
  guarantees or penalties would help make the Guidance more useful and clarify entitlements for
customers. Current ‘Wake Up Packs’ are often impenetrable and full of jargon, leaving customers
  confused and at risk of buying poor products.
— The FCA must require all pension providers to have a duty of care to customers buying retirement
  products, particularly if those products are irreversible, such as annuities. This means making at least
  basic suitability checks and providing risk warnings before selling a potentially unsuitable product.

The principles behind this Bill are, in my view, sound. Sweeping away the draconian restrictions on people’s
pension savings is long overdue and allowing more flexibility is likely to increase the popularity of pensions as
a retirement savings vehicle:

NevertheleSS, there are elements of the proposed legislation which are likely to prove unfair or unworkable
for many pension savers, particularly those who are less wealthy and do not have a financial adviser.

1. REQUIREMENTS FOR CUSTOMERS USING FLEXIBLE ACCESS TO NOTIFY ALL THEIR OTHER PENSION PROVIDERS ARE UNFAIR
   AND UNWORKABLE

This new aspect of the Taxation of Pensions Bill is impractical and will disadvantage many customers. To
insist on people notifying all past pension schemes that they have taken some money under flexible access
would place an impossible or unreasonable burden on too many people. The fines they would face are also
draconian. Many may have only a small sum in an old pension scheme they have lost track of.

This element of the Bill is unworkable and unfair. It is difficult to comprehend why people should be fined
for losing track of old pension entitlements. There are millions of ‘lost’ pension accounts and often people fail
to trace them until they are retired and actually have some time to get their paperwork sorted out. Whilst still
working, many people do not have the chance to go through all their old records or trace all their old pensions
and savings accounts, yet they will face fines of £300 and further daily penalties if they have failed to do so.
If people’s financial affairs are in good order, this would be less problematic, and those who are better off
(and most likely to be able to afford £10,000 a year extra contributions) are likely to have a financial adviser
who helps them with this task, whereas in practice most people with moderate savings do not. These are the
people most likely to have untraced pension accounts, or to struggle to find details of how to inform their other
pension providers. And these were the very people that the reforms were most likely to benefit. Therefore,
imposing such a restriction on them risks undoing some of the advantages of the new regime.

The less-well-off moderate pension savers are more likely to need money from their pension fund but will
find these requirements particularly onerous. Most will have no intention (or ability) to contribute more than
£10,000 a year, but could face fines just because they lacked the time to trace old pension entitlements.

The Government should instead rely on fines for people who do break the new rules. People currently in
flexible drawdown are not forced to notify all their other pension schemes that their Annual Allowance has
reduced to zero. They are fined or penalised if they break the rules. This approach should, in my view, be
adopted for the Money Purchase Annual Allowance.

This notification requirement is apparently designed to minimise losses to HMRC from extra tax relief.
However, allowing people to cash in up to three pension funds of up to £10,000 and retain their £40,000 annual
allowance is likely to result in far more tax leakage than from people failing to notify past schemes about
flexible access and reduce MPAA.

Therefore, I believe the provisions of this Bill need to be amended. Ideally, the requirement to notify all other
schemes should be removed. Alternatively, people should only be required to notify new schemes which they
establish, or other pension schemes into which they are currently actively contributing (contributions made
within the past 24 months perhaps).

2. ADMINISTRATORS SHOULD BE REQUIRED TO USE A STANDARD FORM TO NOTIFY CUSTOMERS ABOUT THE LOWER MPAA
   AFTER FLEXIBLE ACCESS SO THEY UNDERSTAND WHAT IS BEING SAID

Administrators will have to provide pension savings statements for members who have accessed their
pensions flexibly, but can design their own communications. There is a significant danger that these will be
unintelligible for most customers. They may have no idea what they are being told and then fail to act as
they should, and ultimately face fines. I would like to see a standard official form that can be used by every
company, rather than allowing each one to report in their own way. The form should explain the situation in
plain English. Otherwise there is a danger that customers will simply not understand the language that providers will use in these communications. For example, telling them

‘You have now taken an Uncrystallised Pension Fund Lump Sum or have withdrawn money from your flexi-access drawdown account. As your pension fund has been accessed flexibly, we are obliged to tell you that you are now obliged to inform all other pension providers of schemes in which you have accrued pension entitlements that you have a reduced Money Purchase Annual Allowance of £10,000 (however if you have a defined benefit pension scheme your annual allowance for such accruals is £30,000) You are now under a duty to notify all past or present pension providers in which you have rights that you have accessed this pension fund flexibly. Who will understand that?

Plain English version could be more like:

‘As you have taken more than your tax free cash from your pension fund (it’s called ‘flexible access), you can’t put more than £10,000 year into future pensions (although you can put in up to £30,000 into your employers final salary or defined benefit scheme if you have one). You must now tell every other company you have ever had pension savings or pension rights with, that your future pension contributions are restricted.’

This is more likely to be intelligible to the lay person, but of course consumer testing can refine the wording of standard forms to be as user-friendly as possible.

3. GOVERNMENT SHOULD CONSIDER TIGHTENING THE RECYCLING RESTRICTIONS, SO THAT FUTURE PENSION CONTRIBUTIONS CAN LESS EASILY BE USED FOR TAX AVOIDANCE, RATHER THAN GENUINE PENSION ACCRUAL

If the Government is concerned about tax leakage, it should consider tightening the rules around pension recycling, so that those contributing to pension funds after taking any money from their pensions, whether tax free lump sum or flexible access, should have genuine pension-related, rather than tax-related, reasons for further pension contributions.

4. THE BILL SHOULD REQUIRE PENSION SAVINGS STATEMENTS TO BE SENT TO ALL CUSTOMERS IN A STANDARD FORMAT, LISTING THEIR ACCRUED ENTITLEMENTS AND SCHEME FEATURES

The Taxation of Pensions Bill requirement for a pension savings statement to be sent by every scheme after flexible access could also form the basis on which pension providers can be required to produce a standard official statement for every customer approaching scheme pension age. The Wake Up Packs sent out 6 months before pension age should contain a standard form that records the customer’s pension details—i.e. account balance, any penalties that may apply, the charges that are taken, any guaranteed annuity rate attached or any other special features. With this standard information, customers can take a clear record of their pension entitlement to the Guidance session or use the information to assess their options. Currently, the materials sent to members as the Wake Up Pack are impenetrable, far too long and full of words most customers do not really understand. A standard official form recording the essential pension information on one page would clarify the position and help people make better decisions.

5. THE BILL NEEDS TO TACKLE THE PROBLEM OF PROVIDERS FAILING TO INFORM CUSTOMERS CLEARLY WHEN IT COMES TO THEIR PENSION OPTIONS. PUTTING A DUTY OF CARE ON PROVIDERS TO SEND OUT CLEAR STATEMENTS AND TO MAKE SUITABILITY CHECKS AND CLEAR RISK WARNINGS BEFORE SELLING ANY PRODUCTS FOR PENSION WITHDRAWALS WILL HELP TO AVOID CONSUMER DETRIMENT.

Currently, pension providers can sell decumulation products to customers without any requirement to take care about the suitability of that product for that customer. Not even basic suitability checks (such as asking about someone’s health before selling them a standard product that assumes they are in good health, when in fact they may have a serious illness). As there are likely to be more products in future and as some of them will still be irreversible or carry new types of risk, the company selling the product should be required to make at least some basic suitability checks and provide risk warnings to customers before selling them any product. In particular, asking about health and any unpensioned partner, as well as work status, should be mandatory. If people are still working, they are likely to benefit from just leaving their pension fund to accrue additional investment returns, but if they do not realise they have that option they may buy a product they do not need. Too many firms have sold unsuitable products to unsuspecting customers, but because they were not required to ask any questions, the company can claim the product had been mis-bought, rather than mis-sold. A duty of care requirement and basic suitability checks or risk warnings could prevent such consumer detriment. It is simply not enough to rely on the Guidance to protect customers. An extra layer of regulatory protection must be introduced, especially after such fundamental changes and the past market failures.

For these pension reforms to work properly, people must be able to make best use of their pension savings in later life. This will often mean leaving money in the Fund, rather than withdrawing it. Reaching pension age should not necessarily trigger fund withdrawals or flexible access, especially for those with other pension funds or who are still working. The past regime too often drove people, who did not need to take any money, to withdrawing funds earlier than they should and buying unsuitable or expensive products. In future, the pension
regime needs to help people recognise the benefits of leaving money in their pension fund till they really need it, rather than taking it out.

November 2014

Written evidence submitted by Stephen Ward (TP 04)

1. ABOUT THIS SUBMISSION

1.1. This submission is made by Stephen Ward who has been a pensions practitioner since the 1970’s and who specialises in matters relating to overseas pension schemes and their interaction with UK pension schemes.


1.3. This submission is confined to a consideration of the need to amend the definition of a Recognised Overseas Pension (ROPS) to enable those with UK tax relieved pension funds which have been transferred to a Qualifying Recognised Overseas Pension (QROPS) to benefit from the same flexible benefits regime (where local legislation permits) as will apply to members of UK defined contribution pension schemes from April 2015 following the passage of the Taxation of Pensions Bill 2014-15.

1.4. In summary this submission sets out the two places in current legislation where that legislation prevents those who transfer to a QROPS benefiting from a flexible benefits regime.

2. INTRODUCTION

2.1. A pension transfer is the movement of an individual’s accrued pension rights from one pension scheme to another. UK tax legislation specifies which transfers may be made without adverse tax consequences. These transfers are known as “recognised transfers” (Finance Act 2004 s169), and are a type of authorised member payment. The term “authorised member payment” means that this is a type of transaction that can be made without any tax implications on the member or on the transferring scheme.

2.2. To be an authorised member payment such transfers must be made to either a UK registered pension scheme or to an overseas pension scheme which is recognised by HMRC as a Qualifying Recognised Overseas Pension Scheme (QROPS).

2.3. A ROPS is an overseas pension scheme that meets the requirements prescribed under The Pension Schemes (Categories of Country and Requirements for Overseas Pension Schemes and Recognised Overseas Pension Schemes) Regulations, (SI 2006/206 as amended by SI 2012/884).

2.4. A QROPS is a ROPS which makes certain undertakings to HMRC. This includes an undertaking to comply with prescribed information requirements to be found in The Pension Schemes (Information Requirements—Qualifying Overseas Pension Schemes, Qualifying Recognised Overseas Pension Schemes and Corresponding Relief) Regulations, (SI 2006/208, as amended).

2.5. This submission considers the current position as it relates to, and is now inconsistent with, the UK position applicable from April 2015 under the Taxation of Pensions Bill 2014-15.

3. WHAT MAKES AN OVERSEAS PENSION SCHEME A ROPS AND TAXATION OF PENSIONS BILL 2014-15 CONSIDERATIONS

3.1. There are three tests that an overseas pension scheme must satisfy in order to be a ROPS. (SI 2006/206 as amended by SI 2012/884).

   It must be:
   — A pension scheme then.
   — An overseas pension scheme then.
   — A recognised overseas pension scheme.

3.2. A pension scheme

   A scheme designed to provide benefits in respect of retirement, ill-health, death or similar circumstances.

3.3. An overseas pension scheme

   For a scheme to be classed as an overseas pension scheme under Section 150(7) Finance Act 2004, it must be a pension scheme that is established outside the United Kingdom. Normally a pension scheme will be treated as established in the country where its registered office and main administration is. In addition the overseas pension scheme must meet the requirements set out in SI 2006/206 as amended by SI 2012/884.

   The overseas pension scheme must meet the “regulation requirements' test" and the “tax recognition test".
3.3.1 The ‘Regulation Requirements test’

The regulation requirements test is met if **one of the following three requirements is satisfied:**

**Requirement (a)**

1. The scheme is an occupational pension scheme,
2. There is in the country or territory in which it is established a body which regulates occupational pension schemes and
3. The scheme is regulated by that body.

**or**

**Requirement (b)**

1. The scheme is not an occupational pension scheme
2. There is in the country or territory in which it is established a body which regulates pension schemes other than occupational pension schemes and
3. It is regulated by that body

**or**

**Requirement (c)**

Neither requirement (a) or (b) is met by reason only that no pensions regulatory body exists in the country or territory and, either,

1. The scheme is established in a Member State of the European Union or in Norway, Iceland or Liechtenstein, or
2. The scheme’s rules provide that at least 70% of a member’s UK tax-relieved scheme funds will be designated by the scheme manager for the purpose of providing the member with an income for life. The pension benefits payable to the member (and any associated lump sum) must be payable no earlier than age 55 other than in ill health.

**Submission 1.**

We submit that requirement (c) (2) should be amended so that the “70% rule” be deleted so that this requirement only states that, “The pension benefits payable to the member (and any associated lump sum) must be payable no earlier than age 55 other than in ill health.”

This amendment enables an overseas pension scheme to offer flexi access drawdown and uncrystallised funds pension lump sums so long as local legislation permits.

To be consistent with UK legislation the “no earlier than age 55...” provision should be introduced into requirements (a) and (b).

3.3.2. The ‘Tax Recognition’ Requirement

The pension scheme needs to be ‘recognised for tax purposes’ under the tax legislation of the country or territory in which it is established. This requirement is met if **all the of following 3 conditions are met:**

**Condition 1**

The scheme must be open to persons resident in the country or territory in which it is established.

**Condition 2**

The scheme is established in a country or territory where there is a system of taxation of personal income under which tax relief is available in respect of pensions, and **one of tests** (a), (b) or (c) is met.

(a) Tax relief is not available to the member on contributions made to the scheme by that individual or, if the individual is an employee, by their employer in respect of earnings to which benefits under the scheme relate,

**or**

(b) The scheme is liable to taxation on its income and gains, and is a complying superannuation plan as defined in section 995-1 (definitions) of the Income Tax Assessment Act 1997 of Australia,

**or**

(c) All or most of the benefits paid by the scheme to members who are not in serious ill-health are subject to taxation.
Condition 3

The scheme is approved or recognised by, or registered with, the relevant tax authorities as a pension scheme in the country or territory in which it is established.

3.4. A Recognised overseas pension scheme (ROPS)

Under section 150(8) Finance Act 2004 a ROPS is an overseas pension scheme that meets the following requirements prescribed under SI 2006 206 as amended:

It must satisfy:

1. The benefits exemption test,

and

2. One of conditions (a), (b), (c) or (d).

3.4.1 The benefits exemption test

Where an exemption from tax in respect of benefits paid from the overseas pension scheme is available to members of the scheme who are not resident in the country or territory in which the scheme is established, the exemption must,

(i) Also be available to members of the scheme who are resident in the country or territory; and

(ii) Apply regardless of whether the member was resident in the country or territory, when the member joined the scheme; or for any period of time when they were a member of the scheme.

If there is no exemption from tax available to members who are not residents in the country or territory where the scheme is established then the benefits exemption test will be met.

3.4.2 The Conditions

The overseas pension scheme must:

(a) Be established in a Member State of the European Union, Norway, Liechtenstein or Iceland, or

(b) Be established in a country or territory, other than New Zealand, with which the UK has a Double Taxation Agreement that contains exchange of information and non-discrimination provisions, or

(c) Satisfy the requirement that, at the time of the recognised transfer, the rules of the scheme provide that:

(i) At least 70% of the funds transferred will be designated by the scheme manager for the purpose of providing the member with an income for life,

(ii) The pension benefits (and any associated lump sum) payable to the member under the scheme, to the extent that they relate to the transfer, are payable no earlier than age 55.

(iii) Membership of the scheme is open to persons resident in the country or territory in which it is established,

or

(d) Satisfy the requirement that, at the time of the recognised transfer the transfer is made to a pension scheme which is a KiwiSaver scheme as defined in section 4(1)(interpretation) of the KiwiSaver Act 2006 of New Zealand.

Submission 2

We submit that requirement (c) (i) “the 70% rule” should be removed.

This amendment then enables an overseas pension scheme to offer flexi access drawdown and uncrystallised funds pension lump sums so long as local legislation permits.

The “other than New Zealand” provision in (b) becomes redundant.

And arguably (d) also becomes redundant.

November 2014

Written evidence submitted by Mark Hattersley (TP 05)

1. I have been involved in Financial Services since 1979, during this time I have worked for UK trust based pension schemes in an administrative capacity, financial advisory and technical support. During my time as a UK based financial advisor I was registered with the FSA as a Pensions Specialist being a holder of the G60 qualification administered by the Chartered Insurance Institute. I am a Chartered Financial Planner, Certified Financial Planner (both here in the UK and in New Zealand); I also hold the designation of Fellow of the Institute of Financial Planning of which there are currently less than 100 in the UK. I am currently involved
in the International Pensions market, specifically as a business development manager and technical officer focusing predominantly on Qualifying Recognised Overseas Pensions Scheme (QROPS) for a New Zealand domiciled Superannuation Scheme.

2. I wish to make a submission addressing just one issue that revolves around Statutory Instrument 884/2012, which imposed further requirements on schemes wishing to be regarded as an overseas pension scheme and hence a constituent in deciding if the scheme could be registered as a QROPS. This Statutory Instrument made amends to those originally laid out in SI206/2006. In particular I should like the committee to consider governing regulations on those schemes not administered by a provider operating within the European Union or established in a country with which the UK has a Double taxation Agreement (other than New Zealand), which required such schemes to utilise 70% of funds transferred to provide an ‘income for life’. ‘Income for life’ took its meaning from Finance Act 2004. Given the new found flexibilities envisaged from April 2015, I believe the ‘income for life’ requirement should now be dropped from any future taxation provisions and in particular with regards to the provisions regulating New Zealand Superannuation Schemes. As the committee may be aware, the UK and New Zealand have signed up to a particularly strong tax treaty; not only setting out the jurisdiction with taxation rights on taxable revenue and income arising but also calling upon each country to collect any unpaid taxes from its residents on behalf of the other country and to remit those funds to the originating country.

3. The provisions included in SI 884/2012 was an attempt by HMRC to accommodate the fact that New Zealand’s taxation system for Superannuation and KiwiSaver schemes (the two types of retirement focused savings vehicles in New Zealand) is T/T/E. (The Guidance Notes attaching to the Taxation of Pensions Bill reflects upon the UK system of taxation in Guidance Note 5). Following the passing of SI884/2012 members of such schemes could no longer access all funds upon retirement. The provisions under review now allow individuals access to all savings subject to tax being accounted for on the ‘income’ element of each payment.

4. As a consequence of point 3 above, I believe it appropriate for the retention of the requirement that 70% of funds transferred should be identified as providing income, in order to ensure that the member accounts for an appropriate amount of tax on the ‘income element of each payment received from a QROPS scheme in the country the member is tax resident and receives the benefits.

5. I do not believe such changes, if included within regulations, will result in abuse or outcomes not in line with current government thinking or indeed result in any noticeable loss in UK tax revenues, given that according to HMRCs December 2013 update the UK has the largest number of tax treaties in the world numbering, at that time, some 120 such agreements. Completion and submission of the requisite form attaching to Help Sheet 304 would ordinarily exempt such payments fro a UK Pension arrangement from UK taxation at source.

6. Failure to make such amends will have, what I believe to be, unintended consequences not least:

7. Failure to remove the special provisions relating to New Zealand schemes and non EU countries will result in an uneven playing field in international markets, pushing investors into solutions based more about retention of flexibility than, say, pricing, the availability of appropriate investment solutions or indeed taking account of local regulations and the provisions of a DTA that might result in penal taxation for the member in the future.

8. Bring about an unbalanced domestic market place in New Zealand; forcing investors into a decision making dilemma between retention of funds in the UK that will allow them to access flexible retirement benefits from (currently) age 55 onwards (in line with UK residents), but accepting these will be subject to local taxation on both the tax free lump sum as well as suffering higher rates of personal taxation on the income received each year, or agreeing to jeopardise their lifetime goals and financial security by tying funds up in a KiwiSaver Scheme. KiwiSaver schemes ordinarily permit access from State Retirement Age (currently 65 but likely to rise over the long term) but to ones entire fund and without further personal tax liability this is as a consequence of New Zealand’s system of taxation for local residents of T/T/E. “Income for life’ took its meaning from Finance Act 2004. Given the new found flexibilities envisaged from April 2015, I believe the ‘income for life’ requirement should now be dropped from any future taxation provisions and in particular with regards to the provisions regulating New Zealand Superannuation Schemes. As the committee may be aware, the UK and New Zealand have signed up to a particularly strong tax treaty; not only setting out the jurisdiction with taxation rights on taxable revenue and income arising but also calling upon each country to collect any unpaid taxes from its residents on behalf of the other country and to remit those funds to the originating country.

November 2014

Written evidence submitted by Towers Watson (TP 06)

TAXATION OF PENSIONS BILL: WRITTEN EVIDENCE TO PUBLIC BILLS COMMITTEE

Towers Watson is a global consulting company with particular strength in the area of UK pensions. We have advisory relationships with the trustees and sponsors of over half of the 100 largest corporate pension schemes and also schemes ranging down in size to £10m and less.

The Budget flexibilities for delivery of defined contribution (DC) pension savings were bold and pave the way for better member outcomes. They have been broadly—and rightly—welcomed.

Much of the finer detail is still awaited and, with an implementation date of 6 April 2015, this is presenting a challenge for pension providers—whether retail or ‘traditional’ occupational schemes—to deliver those
flexibilities. However, this was inevitable and we commend the Government for not rushing to implement ill-thought-through tax ‘solutions’. We have been in correspondence with HMT, DWP and HMRC on matters of detail.

This submission focuses on a single issue within the Taxation of Pensions Bill—the effectiveness of the anti-avoidance measures and their impact on the durability of the new regime. Two specific measures exist:

1. A reduction to the threshold (£12,500 to £7,500) from which the tax-free cash recycling rules can apply. This is a motive-based test and, although in force since April 2006, we understand that it has rarely, if ever, been used. We do not believe that this is because it is an effective deterrent; rather we believe that it is (and will remain) unenforceable.

2. Once DC savings have been flexibly accessed, the annual allowance (AA) for future DC savings reduces to £10,000.

This latter provision is mechanistic and, at least in principle, a more effective deterrent. It is intended to dissuade individuals aged 55+ from repeatedly (annually) diverting up to £10,000 of salary into immediately-accessible pensions and drawing those savings immediately. In such circumstances, one quarter of the income saved would become tax free and, if structured as a salary sacrifice arrangement, National Insurance Contribution savings would be available to both the employer and employee.

We agree that this will be a robust deterrent for those who might otherwise wish to contribute more than £10,000 to DC savings in a year. However, according to the Government\(^1\) this covers less than 2% of DC savers aged 55+, leaving 98% who could reduce their tax bill (though some of these may want to increase pension savings once they can access money flexibly in retirement).

Ministers, at times, appear sanguine on this matter—“we have tried to ensure that we do not give people an opportunity to use the new arrangements as a way of avoiding substantial amounts of tax … [and] concluded that introducing a reduced £10,000 personal allowance was the best way of striking a balance …”\(^2\) However, the Financial Secretary to the Treasury’s evidence to the Committee on 11 November seemed to bolster previous warnings that “the government will be closely monitoring behaviour under the new system”.\(^3\) In his evidence, the Minister suggested that, if loss accelerates, action will be taken.

We are concerned that such acceleration—and the implied response—is likely; we are not reassured by the suggestion that few people will be tempted to try to get the tax benefits that are attached to retirement saving without actually saving for retirement. There are around 9m people over 50 in employment. Of course some of those will be younger than 55 or working part-time and earning very little. Some will be put off by the administrative inconvenience of making contributions and withdrawing them. And some will already be saving without actually saving for retirement. There are around 9m people over 50 in employment. Of course some of those will be younger than 55 or working part-time and earning very little. Some will be put off by the administrative inconvenience of making contributions and withdrawing them.

However, we believe that there may be many people who will consider taking advantage of this opportunity—particularly so if products are designed and marketed with this outcome in mind. With an AA set at £10,000, the maximum income tax gain on offer through an immediate-vesting drawdown vehicle might be £300–£400 per year for a basic rate taxpayer (net of say £100–£200 charges) or £800–£900 for a higher rate taxpayer. Moreover, if £10,000 of salary is given up in exchange for an employer pension contribution, the employer could pay £1,380 less National Insurance while the employee would pay between £200 and £1,200 less (this time, higher earners gain less). This may also be something that employees can achieve on their own initiative by collaborating to exploit these already?

It is true that the Budget created scope for some people to avoid tax in 2014-15 and it is equally true that there is little evidence of widespread appetite to exploit it. However, both trivial commutation and small lumps are:

- Available only if the total benefit value is within a cap—£30K across all pension arrangements for trivial commutation and £10K within the scheme for small pots
- Available only to over 60s (rather than 55s from 2015)
- Required to exhaust all benefit entitlement under the scheme (post-2015, schemes could, but won’t be required to, permit members to cash in just part of their pot).

Further, a trivial commutation exercise can be undertaken only once, and it is administratively bureaucratic. So these approaches remain a world away from the avoidance risk created from April 2015 for those aged 55 and over.

---

\(^1\) Paragraph 2.31 of “Freedom and choice in pensions: government response to the consultation” CM 8901, July 2014
\(^2\) David Gauke: Official Report, Pension Schemes Public Bill Committee, 23 October 2014, c. 126, Q284
\(^3\) Paragraph 2.33 of “Freedom and choice in pensions: government response to the consultation” CM 8901, July 2014
The essential point in all this is that it is a tax avoidance opportunity created by legislation currently before Parliament; it is not dreamt up by accountants. Taxpayers and businesses wishing to help their employees with the cost of living should know whether this is supposed to be acceptable tax planning or avoidance to be frowned on (or stopped).

If the Government wishes to ensure that its framework actually delivers better member outcomes, it needs to be encouraging employers and Trustees to invest in supportive financial education. While the guidance guarantee will play a significant part in helping members to understand the choices with which they are (directly or otherwise) presented, a better understanding will be achieved if the ‘at retirement’ guidance is supplemented by broader financial education support, delivered over a longer period.

Businesses and Trustees need confidence that the Government both fully understands the potential opportunities for tax and national insurance ‘avoidance’ and that it has incorporated the associated costs within its planning. Education will have little value if the new system is not durable and faith in the pension system will be (further) eroded if education is provided, only to be undermined by changes introduced to tackle tax avoidance.

There are approaches that would make salary diversion unattractive—such as restricting the tax-free cash ‘entitlement’ attributable to DC savings made after benefits have been accessed flexibly, or setting the annual allowance at zero for people who have done so—but there are considerable drawbacks to all of these and they have already been considered and rejected.

We are not suggesting an about-turn, but it is important that the new regime—which introduces very significant changes—is durable. If the Government is genuinely relaxed about those aged 55+ diverting up to £10,000 p.a. of salary into pension savings (that are then drawn immediately), it should say so. If it is not, then it should explain how it might dissuade this, while maintaining the integrity and cohesion of the new regime.

November 2014

Written evidence submitted by Just Retirement (TP 07)

SUMMARY

1. The Taxation of Pensions Bill introduces major changes to the framework for how people can use their Defined Contribution (DC) pension savings in retirement. These changes should lead to improved outcomes for consumers but this will depend on the success of key provisions within the reforms—especially the Guidance Guarantee (GG) in helping people understand their options and risks at retirement.

2. Just Retirement is increasingly concerned by the risk of low take-up of the GG and the current absence of any regulatory response to address this risk ahead of the reforms’ introduction next April. These concerns have been echoed in recent weeks by leading consumer advocates and industry representative bodies including the Association of British Insurers (ABI).

3. This briefing focuses on those aspects of the reforms which set out the GG framework, provides details on the gaps identified, and suggests remedies which we hope will help Bill Committee members address these failings.

CONTEXT

4. The Taxation of Pensions Bill creates the tax framework that will enable the “freedom and choice” reforms announced in Budget 2014. The improved access available to savers from April 2015 is welcome but brings new risks, including the specific risk of unanticipated income tax charges on sums drawn directly from pension savings.

5. Retirement decisions will be more complex than ever in the new system and consumers will have to understand and choose between an unprecedented range of options. With consumer engagement known to be poor; pension providers’ lamentable track record for selling inappropriate or poor value retirement income products to their existing DC pensions customers; and the likelihood of attempts by some unregulated organisations to exploit vulnerable consumers—the thoroughness of consumer protection measures will be vital. This will be especially important if take up for the GG is low.

6. With less than six months until the reforms are implemented our major concern is that the regulatory regime being created by the Financial Conduct Authority (FCA) and The Pension Regulator (TPR) is incomplete, and will remain incomplete in the absence of safeguards to protect consumers who do not use the GG or receive regulated financial advice.

RECENT DEVELOPMENTS IN THE AT-RETIREMENT MARKET

7. No less than three investigations into consumer detriment in the UK retirement income market have taken place since the Financial Service Authority’s introduction of rules requiring pension providers to disclose the ‘Open market option’ (OMO) in 2002. Annex 1 charts the path of government/regulatory investigations and subsequent industry attempts to improve disclosure through Best Practice Guides and Codes of Conduct.
8. Each industry-led attempt to improve at-retirement disclosures has brought some marginal improvement, but no significant shift in shopping around activity. Despite the sustained efforts of the ABI to coordinate pension providers’ sales and communication practices, the majority of DC pension savers still don’t shop around at retirement.

FCA—CURRENT REQUIREMENTS, THEMATIC REVIEW AND MARKET STUDY

9. The FCA’s Conduct of Business Rulebook requires pension providers to remind their customers of the OMO. Providers are required to flag this option in a “wake-up” pack 4-6 months prior to the customer’s stated retirement date as the spur to action. The wake-up process is being reviewed by FCA to reflect the pension reforms. Following consultation, FCA will shortly set out its intended regulations for the GG and arrangements for how providers will direct consumers to the service—the “trigger” communication.

10. The FCA is also conducting a Market Study into the retirement income market following its February 2014 Thematic Report. This Thematic Review found fewer than half DC retirees had exercised the right to OMO and eight in ten retirees who bought an annuity from their existing pension savings company would have achieved a better deal had they purchased their annuity from the open, competitive annuity market. A majority of ‘internal’ annuity purchases are made on the default option offered—a conventional annuity rate on a single-life basis.

11. The scope of the FCA Market Study was revised following the announcement of the pension reforms in Budget 2014. This will examine competition and choice in the context of the various options open to consumers when retiring, and assess the value for money associated with different at-retirement products. Interim findings from the study are expected in December, with final results in Q1 2015. These findings are not expected to be available to inform the GG regulations FCA is due to publish in December.

GUIDANCE AND THE TAXATION OF PENSIONS BILL

12. In its consultation on the regulatory framework for the pension reforms24 the FCA identified the need for the GG to inform, educate and help consumers understand their options when accessing pension savings. The FCA is incorporating a mandatory requirement for product providers to help consumers understand the income tax implications of withdrawing lump sums from their DC pension savings. However, it has not proposed similar active interventions in relation to product feature choices where people have repeatedly made inadvertent poor choices that have been shown to cause regret and financial detriment in later life.

13. The Taxation of Pensions Bill does not contain the clauses that enable the FCA and TPR to set and regulate the GG—these are contained in Part 4 of the Pension Schemes Bill, shortly expected to go to Commons report stage. However, that Bill and the Taxation of Pensions Bill are closely connected, and Bill Committee members should be aware of the potential harm that will occur if no requirement is placed on product providers to help consumers avoid inadvertent poor decisions.

14. If measures are not taken to address the risk of people accessing DC pensions savings without first taking the GG, the freedoms created by the Taxation of Pensions Bill are likely to be greatly undermined at outset by failing to help consumers to identify a range of known risks. These include:

- Risk of paying too much income tax
- Risk of outliving your assets/running out of money
- Risk of missing out on guaranteed annuity rates from existing company
- Risk of not providing benefits for a spouse/other person on death
- Risk of missing out on additional income resulting from medical conditions or lifestyle factors
- Risk of savings and income erosion from inflation
- Risk of purchasing an uncompetitive product
- Risk of benefiting my combining pension pots
- Risk of paying an exit charge when it could have been avoided

15. These negative outcomes are likely to be exacerbated by the absence of a backstop regulation or ‘second line of defence’ requirement to ensure consumers consider these risks.

16. Concern at this likelihood is growing given that GG take-up could be low. A pilot exercise conducted by The Pensions Advisory Service and the pensions provider Legal & General in May 2014 found that just 4 per cent of 9,000 pension savers took up the option to use a free, impartial guidance service. A separate survey by the Chartered Insurance Institute (CII) found that 44 per cent said they would “definitely” use the GG from April, while 48 per cent said they would “probably” use it.

NEED FOR A SECOND LINE OF DEFENCE

17. Concerns over low take-up of GG has led to calls for a second line of defence requirement to be built into FCA/TPR regulations. A second line of defence regulation would help counteract these potential negative

outcomes—first, by requiring product providers and pension schemes to encourage non-users to use the GG before making decisions about how to use their DC pension savings. Second, it would require product providers to ask mandatory questions to check consumers are aware of the implications arising from how they access their DC pension savings.

18. This would not prevent or impede savers from accessing their savings as they wish—but would merely provide a check against unintended negative outcomes.

19. Just Retirement is concerned by the absence of clear plans to introduce a second line of defence regulation in time for the start of the new freedoms. Pressed on this issue by MPs during last month’s evidence sessions, FCA representatives said GG take-up will be “a matter for public choice”. We believe this position creates great risk for the millions of people who, from April 2015, will be entitled to access DC pensions savings from age 55, despite the fact that FCA and TPR already have powers to implement a second line of defence requirement.

20. As noted in Annex 2, consumer advocates including Dr Ros Altmann (the government’s Business Champion for Older Workers), Sue Lewis (Chair of the Financial Services Consumer Panel), Dominic Lindley (former head of head of personal finance at Which?) and Jane Vass (Head of Public Policy, Age UK) have recently expressed their concern at the FCA’s apparent reluctance to implement these safeguards. The ABI has also called for a second line of defence regulation.

21. Witnesses also argued that the absence of a second line of defence contradicts the FCA’s Treating Customers Fairly principles. These principles set out six core outcomes which the FCA expects of regulated firms, with outcomes 1-3 specified as especially relevant to at-retirement processes. These are:

— Outcome 1: Consumers can be confident that they are dealing with firms where the fair treatment of customers is central to the corporate culture.

— Outcome 2: Products and services marketed and sold in the retail market are designed to meet the needs of identified consumer groups and are targeted accordingly.

— Outcome 3: Consumers are provided with clear information and are kept appropriately informed before, during and after the point of sale.

KEY POINTS

22. The FCA and TPR are expected to publish final rules for the GG framework in December. Both regulators have the powers to create a second line of defence requirement, but there are currently no plans to introduce this safeguard. This contrasts with specific provisions being set in place to ensure consumers are made aware of potential income tax charges relating to withdrawals from DC pension savings.

23. As parliamentarians have already identified failure to address this risk will mean the first wave of retirees are likely to be “guinea pigs”, whose negative experiences come at great personal and financial cost. These negative experiences could greatly undermine the reforms from the outset.

24. The FCA is an independent financial regulator but is accountable to HM Treasury and Parliament. Bill Committee members therefore have the opportunity to press for assurances that this gap in the reforms will be closed in time for the first wave of retirees in April 2015.

ABOUT JUST RETIREMENT

25. Just Retirement is a specialist provider of financial services to people at and in-retirement. We are the UK’s leading provider of individually underwritten annuities, the second largest provider of equity release lifetime mortgages and are among the leading innovators in the care annuity market.

26. We are members of the Association of British Insurers, the Equity Release Council, the Council of Mortgage Lenders, the Pension Income Choice Association and the International Longevity Centre’s Care Funding Advice Network.

November 2014

25 http://www.fca.org.uk/firms/being-regulated/meeting-your-obligations/fair-treatment-of-customers
ANALYSES, ASSURANCES AND PAST ATTEMPTS TO REFORM DC PENSION RETIREMENT PROCESSES

Dr Ros Altmann (Business Champion for Older Workers): “Consumers have been left in the dark and at the mercy of the providers for years. Providers must be required to know who they are selling something to before they sell it. In other words, I believe they must be required to ask some fundamentally important questions of whoever it is they are selling a product to, whether or not that person has had guidance, but particularly if they have not had guidance.

“I would call on the FCA to ensure that providers are required to treat customers properly and fairly, and to have this safeguard so that if you do not get the guidance, someone will at least take notice of your circumstances when you buy a product and help you with what questions to consider before committing.”

Dominic Lindley (Consumer rights consultant): “The guidance guarantee is absolutely welcome but unless we take further action and introduce extra lines of defence, you are still going to get insurance companies defaulting people into very poor value products. They have been defaulting people into poor value annuities for years.

“We are kind of relying on the FCA, and as you saw earlier in the week, the FCA does not seem to want to introduce even the second line of defence by getting providers to ask specific questions at the point at which people access their pension.”

http://services.parliament.uk/bills/2014-15/pensionschemes/stages.html
Jane Vass (Age UK): “There is a list of questions, which is not that long and which providers should always have asked and should always have been required to ask but have not asked, and we could now ensure that they do ask them before selling a product.

“If somebody is considering rolling over with the existing provider, again, I think we need safeguards there. I am a bit anxious about the concept of just asking people a list of questions and getting them to tick a box, because we know in the past that sometimes less reputable providers have used that as an opportunity to get people to tick the box and then say, “It wasn’t me, guv. They said they were okay.” In that case, I think we would be looking at building sensible defaults into the system.

Dr Yvonne Braun (ABI): “We are asking the FCA to make its expectations clear that, from next April, providers of retirement income products make customers aware—those customers who have not taken the guidance especially—of a number of risks that they need to be aware of before they buy a product...

“It is not clear whether everybody is going to take up the guidance, so there needs to be some sort of second line of defence—guard rails, back-stops, or whatever you want to call them.”

Written evidence submitted by Friends Life (TP 08)

1. This submission has been prepared by Friends Life in order to highlight issues relating to the Bill which may either lead to consumers being unable to access new freedom and choice in pensions or to poorer outcomes as a result of that access. It also suggests how those issues might be mitigated.

2. The rules governing pensions are complex. The new freedoms whilst welcome increase the complexity for consumers further. Whilst some of the details below are quite technical, they may have adverse impacts for a range of consumers. This risk exists, not simply for wealthy people who can afford to pay for significant amounts of professional support, but also for ordinary people with much smaller pots.

3. Friends Life is the second-largest provider of workplace DC pensions in the UK and manages funds of £117.6 billion (as at 31 December 2013) on behalf of our customers. We want our 5 Million customers to have the best standard of living possible in retirement and propose public policy reform that seeks to deliver that aim.

(i) Pension Transfers—loss of pre A-day protection

4. Background: A large number of pension scheme members have protected (higher) tax free cash sum entitlements resulting from membership of schemes prior to 06.04.2006 (A-day). Others have a protected retirement age lower than the current normal minimum age. These protections are lost on transfer to another scheme other than ‘block transfers’ (where at least two members are transferring simultaneously). Following the Budget 2014 announcements, a transitional easement was granted whereby protections would be retained even if only one person was transferring. This was to enable people in old inflexible schemes to transfer to schemes that will offer the new options. However this easement only extends to 5 April 2015. Beyond that the original block transfer rules will apply.

5. Issue: Friends Life is aware that for commercial reasons many providers will only be able to offer full flexibility through a limited range of products. Many pension scheme members will therefore need to transfer between products if they wish to take advantage of the new flexibility and choice post 5 April 2015. However any transfers made after that date could result in the loss of protected benefits. This seems an unfair outcome and not consistent with the Government’s policy of making pensions flexibility widely available.

6. Mitigation: We believe that the current easement on block transfer rules should extend indefinitely beyond 5 April 2015.

(ii) Short Term Annuity Rules

7. Issue: The short-term annuity rules as they stand are unnecessarily restrictive. They mean a fixed-term annuity of longer than 5 years can only be written within a drawdown arrangement. Writing an annuity product under the drawdown rules adds cost and complexity. The costs need to be reflected in the pricing of the product which in turn makes it a less attractive proposition for consumers. The limitation on the length of a short term annuity is therefore stifling product innovation and leading to unmet consumer needs. In particular a fixed term annuity might be required to bridge a period between cessation of work and the commencement of another pension, such as a defined benefit scheme or the state pension.

8. Mitigation: It is suggested that the short term annuity rules are amended to allow a fixed term annuity of any length. If this is problematic and since the normal minimum pension age can never be more than twelve years ahead of state pension age, a twelve-year maximum (if there has to be a maximum at all) would be a significant improvement for consumers.
(iii) Permissive Scheme Rule Override

9. **Background:** Pension scheme rules establish the legal framework by which schemes operate and reflect the underlying pension legislative regime. However substantial amendments to scheme rules can be expensive and time-consuming. As a result the Government is introducing a permissive override that will allow scheme managers/trustees to offer flexible access to pensions even if the scheme rules do not permit this.

10. **Issue:** As it stands, the draft legislation does not extend the override to the following:

   — The reduction in the age at which a member can commute small pensions (from 60 to 55)
   — The facility for any beneficiary to take income from an inherited drawdown fund following the death of a member (currently only dependants can do this).

11. **Mitigation:** We would encourage a review of the permissive scheme override to ensure there are no obstructions to accessing pension flexibility.

(iv) Designation of Drawdown Funds

12. **Background:** Many existing drawdown pension products are structured so that if new funds are applied (“designated”) to a member’s pension drawdown fund, the funds are applied to a new arrangement. However the draft legislation requires that, by default, the new funds must be treated as flexi-access drawdown funds.

13. **Issue:** This means that a consumer who joined a scheme pre 6 April 2015 and uses their existing capped drawdown facility will not be able to designate new funds to the capped drawdown product and will be forced down the flexi-access route. This in turn will trigger the restricted money purchase annual allowance (of £10,000). HM Treasury has suggested that providers can re-structure products to overcome this issue. We do not believe this will be practical due to system and time constraints and changes to product terms and scheme rules possibly requiring customer consent.

14. **Mitigation:** We are focussing on other solutions for our customers, but believe it would be better for consumers if the legislation was more accommodating. In particular, Friends Life suggests that pre 6 April 2015 members who have existing capped drawdown arrangements under a scheme should be given the option to determine that any future designations of funds to new drawdown arrangements within that scheme are applied as capped drawdown not flexi-access drawdown. We believe that this would lead to fairer outcomes for consumers.

15. A similar issue arises with designation of drawdown funds to a beneficiary/dependant following death of a member. Legislation requires that the designation must be applied to the originating scheme and must also be applied in the form of a flexi-access drawdown. This approach creates a problem if the product does not offer a flexi-access facility. Friends Life suggests amending the Bill so that funds inherited on death from an existing capped drawdown arrangement may also be applied to a dependant’s capped drawdown.

November 2014

---

**Written evidence submitted by Talbot and Muir (TP 09)**

**CONTEXT**

1. Talbot and Muir is a self invested pension plan (SIPP) and small self administered scheme (SSAS) provider, formed in 1993. We are fiercely independent and provide pensions administration services to individuals via their financial advisers.

2. Claire Trott, Head of Technical Support at Talbot and Muir spends the majority of her time talking with, and presenting to, regulated financial advisers so has a clear insight into the issues they are experiencing with their clients on a day to day basis.

3. The following is based on discussions with financial advisers since the announcements in the 2014 Budget.

**ABOLITION OF CAPPED DRAWDOWN FOR NEW ENTRANTS FROM APRIL 2015**

1. Capped drawdown is a well understood concept in the pension profession, generally recommended by financial advisers, rather than purchased directly by the client.

2. The removal of capped drawdown as a retirement option for individuals, after 5th April 2015 will be detrimental to a small but significant number of pension savers in the UK.

3. We have heard from advisers that clients like the option of retaining a government based calculation of maximum income particularly if it does not trigger the money purchase annual allowance rules.

4. Capped drawdown is remaining for those already in receipt of benefits in this form, so providers, such as our company, will continue to provide these options as long as they are needed. So this is creating a two-tier system.
5. Clients who are not eligible to enter capped drawdown before 6th April 2015, will be penalised when they take income because they will be hit by the newly introduced money purchase annual allowance rules, whereas those eligible to enter capped drawdown by the end of this tax year will be able to contribute more to their pensions in the future should they wish.

6. Due to the age restrictions on taking benefits, people are being penalised with the new contribution rules just because they are unable to act this tax year. Those able to act now will continue to benefit from the higher annual allowance as long as they don’t break the maximum income allowance.

7. The 150% of the GAD tables, based on age and fund size used will need to be kept under constant review should you choose not to abolish the capped drawdown rules to ensure it is reasonable that those using it will not be taking excessive advantage of the contribution rules.

8. It should be noted that the requirement to keep capped drawdown as a retirement option goes hand in hand with the fact that it will not be a trigger for the money purchase annual allowance rules.

**Transfers of Capped Drawdown**

9. Transfers of capped drawdown need to be segregated from uncrystallised funds and the maximum income maintained using the calculations from the previous providers. They cannot transfer as a partially crystallised arrangement.

10. Once transferred any uncrystallised funds will not be eligible under the current proposals to enter capped drawdown, the only option to access drawdown will be flexi-access drawdown.

11. By accessing flexi-access drawdown, the money purchase annual allowance rules will be triggers as soon as any income is taken.

12. This is a detriment to those that are with a poor performing provider or one that increases their charges in the future.

13. This could be resolved by allowing capped drawdown to remain for new designations without triggering the money purchase annual allowance rules.

**Background Information**

14. Many clients with SIPPs and SSAS are small/medium business owners, whose only substantial accessible cash could be their pension, assuming they are over 55.

15. We have seen clients who have needed to access their pensions earlier than they wanted in order to help their business with an injection of capital in hard times. They have been unable to obtain loans to the company so this has been their only option. Although part of this would be tax free some is likely to be taxable at their marginal rate. Clients at a later date wish to add further funds to their pension and have done so they can continue to fund for their retirement as originally planned.

16. This has two benefits; firstly the small business owner is still able to provide for their retirement. Secondly, the business has been able to continue to make a meaningful contribution to the economy.

17. In order to make contributions to a pension and receive personal tax relief an individual needs taxable income, pension income although taxable is not counted towards this so there is little danger of recycling of income.

18. There were clearly no issues with recycling pension income using capped drawdown prior to the announcement of new pension flexibilities.

**Comments Obtained from Financial Advisers**

19. Carl Lamb, Almary Green—It seems nonsensical to me that my clients are being penalised by restricting their retirement options with the removal of capped drawdown meaning the only way to take drawdown income will trigger the MPAA rules. I can see a situation where a client that has previously needed to access some income, receives a redundancy payment but will be limited to using just £10,000 as a pension contribution, rather than £40,000 because of the additional restrictions, but all they want to do is protect their retirement income. I would urge a rethink on capped drawdown to ensure that this remains in place.

20. Chris Bowmer, Fortitude Financial Planning—People who are prepared to restrain their withdrawals should be allowed to do so without suffering from a lower annual allowance. If the Government is going to allow people to remain in capped drawdown, why not let them continue to enter it if they want to? You’ve still got the two sets of rules; you might as well keep them for everybody. People don’t know what their future is going to bring them. To commit to one course of action goes against the whole spirit of the new rules.

21. Jamie Smith-Thompson, Portal Financial—The Government needs to create a rule that is fairer for everyone. Introducing a change that will allow certain people to contribute four times as much as other people is manifestly unfair and could prompt people to feel punished for the year in which they access their fund. This change is so big it is easy to envisage a surge in capped drawdown between now and April and the Government should take this into consideration and create a rule that is fairer for everyone involved.
22. **Paul Stocks**—I do agree that having capped drawdown as an option post April 15 makes sense—and I agree that maintaining a 150% GAD is perhaps too high (it was only a temporary fix) for those who are looking to maintain income until death. I’m all for choice and therefore having the option of Flexi with a £10k AA or Capped and a £40k AA would do just that...

**CONCLUSION**

23. Capped drawdown should remain an option for all those wanting to use it.

24. The use of capped drawdown, provided individuals remain within the GAD limits, should not trigger the money purchase annual allowance rules.

*November 2014*

**Written evidence submitted by John Greenwood, pensions journalist (TP 10)**

**INTRODUCTION**

— It is undeniable that the new pension freedoms create the potential for avoidance of income tax and employer and employee NI on a massive scale. With full access to their pension, over 55s can be remunerated far more efficiently through pension contributions (no employer or employee NI and 25% tax-free) than through salary.

— There is no definitive figure for the full scale of the Treasury’s exposure (if everyone maximises their ability to avoid tax and NI). I calculate it as being in the region of £20bn in 2015/16. It could be £25bn, it could be £15bn. Nobody expects this entire sum will be lost to the public purse, but it is possible that at least 10% per cent of the overall exposure figure, whatever it may be, could be lost in 2015/16.

— Nowhere in the Budget or the policy costings document published alongside it is there any mention of the potential loss of NI. The Treasury’s exposure to NI loss through over-55s flushing salary through pension is five times bigger than its exposure to income tax loss through this strategy.

— The only publically available evidence of the extent to which employers and employees will exploit the tax and NI avoidance opportunities of the new rules suggests that significant numbers intend to do so.

— The pensions minister cross-examined me at length in the Pension Schemes Bill committee on my £20bn figure, but has been unable to confirm what the government’s estimate is, or even that he has seen a government estimate of the potential lost revenue through increased use of salary sacrifice. A Freedom of Information Act request made by my magazine in July 2014 asked for details of assumptions of increased use of salary sacrifice in calculating the fiscal impact of the changes. No substantive response has been forthcoming.

— These factors suggest that the government had not spotted the loophole when it launched the policy. Its attempt to close the loophole, the £10,000 annual allowance for those who access flexible drawdown is, by the Treasury’s admission, only a deterrent to 2% of the population. The limited evidence available suggests a significant loss to the public purse if the Bill goes through in its current form.

1. I am editor of Corporate Adviser magazine, a magazine for pensions consultants. I am also the author of the FT Guide to Pensions and Wealth in Retirement, former deputy personal finance editor of the Sunday Telegraph and a frequent freelance to several national newspapers.

2. Some of the opinions in this submission have been included in an earlier submission to the Pension Schemes Bill.

3. The unprecedented liberalisation of the process for withdrawing pensions, outlined in the Budget 2014 and taken forward within the Pension Schemes Bill, creates huge new areas of potential tax leakage that appear to have been completely missed by the Treasury, the Office for Budget Responsibility and those advising them. It is in this area that I believe I have information and understanding that will be of particular interest to MPs debating this bill.

4. The Treasury’s prediction of £3bn extra tax revenue resulting from its freedom and choice in pensions policy, set out at Chart 1.11 in the 2014 Budget document, appears wildly inaccurate— I believe the Treasury will lose much more money than it will gain. I also believe the Budget papers show the Treasury was not aware of this issue at the time the Budget was delivered, despite claims from Treasury officials and pensions minister Steve Webb to the contrary.

5. The freedom to access pots entirely once an individual reaches age 55, creates an opportunity for anyone over that age to avoid liability for both employer and employee National Insurance, as well as income tax.

6. I have calculated that in excess of £20bn could be lost in the first year of this new policy if everyone over 55 takes advantage of this new option. I have presented this figure to numerous experts in the pensions industry, and none have suggested that the potential loss is not of something of that order. In the course of my job I regularly speak to the most senior professionals in the pensions industry and I am yet to get a kickback on
the figures I have put forward. I do not believe that everyone over 55 will take advantage of this loophole, but even if 10 per cent do, that is still a £2bn loss in the first year, a considerably worse outcome than the £300bn net gain predicted by the Budget documentation.

7. I would caveat this statement by pointing out that I am not a researcher or an analyst. However, remarkably, no other organisation has published figures attempting to quantify the loss of NI and tax through this policy. I am happy to be corrected as to the accuracy of these figures. I originally estimated the total potential tax loss figure, with assistance from industry professionals, at £24bn, a figure that appeared in the Telegraph newspaper on May 29, 2014. I believe that £20bn is probably closer. This is on the basis of every one of the 5m or so people over age 55 and below state pension age taking advantage of the loophole.

8. I also accept a point made by David Gauke MP in a memorandum from HM Treasury to the co-chairs of the Pension Schemes Bill Committee on the £10,000 annual allowance, dated 3 November 2014, that individuals over age 55 wanting to take advantage of a full £40,000 contribution in their first year would need other assets to live on until the end of the year before being able to access their pension, because making monthly withdrawals would trigger a reduction of their annual allowance to £10,000. It is uncertain how many of these high earners would have other assets to live off, enabling them to maximise their tax and NI avoidance.

9. But even if the risk to the Treasury is half my figure, and I am yet to hear anyone suggest this to be the case, then a 10 per cent take-up would still amount to £1bn loss in 2015/16, more than wiping out the £320 gain predicted by the Budget.

10. The Treasury has published measures to restrict tax leakage, which by my reckoning reduce the potential loss per year to around £10bn a year thereafter. But the Treasury’s attempt to close the loophole—the reduced annual contribution allowance of £10,000 pa for anyone taking pension benefits—only reduces the potential for tax leakage for the 2016/2017 tax year—it does virtually nothing to limit tax losses in the 2015/2016 tax year.

11. Here is how it works—under the current rules individuals over age 55 can start drawing their benefits, but, tax-free cash aside, they can only draw cash out at a rate prescribed by the Government Actuary’s Department, because pension must be paid as income. Therefore, anyone who opts to have their entire salary (less minimum wage, which must be paid by law) into their pension, can build up a big pension pot and will avoid a lot of employer and employee NI, but will not have enough to meet their day-to-day expenses.

12. Under the new rules employers can choose to pay employees into two pots, both of which have complete access for those over 55—salary into the current account or pension into the newly flexible pension account.

13. Payments made through the salary channel attract employer NI of 13.8% on everything over £7,956. Employees also pay NI of 12% on everything over £7,956. And employees pay income tax on the entire amount.

14. Payments into pension are free of both employer and employee NI, and a quarter of them can be taken as tax-free cash.

15. Salary sacrifice for pension contributions is legal and the strategy of maximising it has been used for years by senior executives looking to boost their pension contributions in the year before retirement—they have been able to do this under current rules because they tend to have other money to live off, so don’t need the income.

16. Salary sacrifice for regular pension contributions is used by a very large proportion of large and medium-sized companies, as well as DB schemes.

17. By opting to be paid through pension via salary sacrifice rather than 100 percent through salary, an individual on £40,000 could cut their total tax and NI bill almost in half, from £9,845 to £4,997. Factoring in lost employer NI, the total cost to the Revenue would be £5,484, a loss off 62 per cent.

18. Clearly not everyone will do this—many employers will baulk at the complexity. Larger employers may decide it sounds like a wheeze and be worried about reputational risk. But I speak to corporate pension advisers on a daily basis and they say some employers, particularly SMEs will definitely want to go for this.

19. A further avenue of revenue loss is through bonuses. For anyone over, or approaching the age of 55, flushing bonuses through pension will now become the norm. Take the cash through salary and you pay tax and NI on the whole sum, but pay it into a pension and you pay no NI and a quarter of the fund is tax free, and you can still take your money tomorrow.

20. I have made at least six requests to the Institute of Fiscal Studies for some comment, reaction or perspective on the issue and the veracity of my own numbers. They have declined to put someone forward to speak to me, for reasons best known to them.
21. The Government has attempted to close the loophole while at the same time retaining the flexibility of the new reforms, which have proved massively popular with the public. But it cannot do both. Its only lever is the reduced annual allowance for those who take their cash early, but this has been designed so that it does not impact anyone but the highest earners. Earners of all income brackets can save thousands through these new rules. The Treasury’s response to the consultation on these measures actually stated that the £10,000 annual allowance would not affect 98% of the population. So by that same token, it is therefore no deterrent to people taking advantage of this tax avoidance opportunity.

22. In its response to a Freedom of Information Act request from Corporate Adviser, my magazine, for information on the costings and assumptions used in the formulation of the policy, in particular the extent to which increased use of salary sacrifice into pensions had been factored in, the Treasury cited public interest against releasing further details. The only substantive response it was prepared to give was to refer back to the documents published alongside the budget.

23. The budget papers set out an increase in revenue of £320m in 2015/16 rising to £1.2bn in 2018/19. Clearly it has made some assumptions to get to these figures—namely that somewhere south of £3bn more will be taken out through flexible drawdown in 2018/19 than would have been the case if people were using annuities or old-fashioned drawdown, and that income tax will be paid on these sums.

24. The Policy Costings document published alongside the Budget 2014 focuses solely on the number of people who access their money early. The statement ‘this leads to an increase in income tax received in early years as individuals will now pay tax on the withdrawals from their pension pot’ is the only post-behavioural costing factor referred to by the Treasury in the entire paper, other than a single line that says ‘adjustments are also made for the higher costs of pensions tax relief to reflect the increased attractiveness of pension savings for some individuals’. There is no mention of lost National Insurance, the far greater risk to the Treasury, that is central to my submission.

25. Under the Policy Costings document’s heading ‘Areas of uncertainty’, reference is only made to the number of individuals making use of the new withdrawal facility, with no mention of the number of employers that could use it to cut their payroll costs or employees using it to reduce their NI and tax bill. While the Treasury’s refusal to disclose sensitive detailed predictions is to some extent understandable, the fact that there is no mention whatsoever of lost NI through salary sacrifice suggests the issue had not been spotted when the policy was published.

26. The calculations and observations contained in this submission were questioned at length by pensions minister Steve Webb MP, but he has been unable to confirm whether he had

26. Financial secretary to the Treasury David Gauke said in evidence to the committee that HMRC “would want to monitor any fiscal risks. If we identified it as something that could be costing the general taxpayer significant sums of money, that’s something we would want to address. Clearly, it’s in the interests of the general taxpayer that it’s not exploited.”

27. The Treasury’s position seems to be that the £10,000 reduced annual allowance is sufficient deterrent to stop abuse of the rules, and provided not many people do abuse the rules, it will not do anything. However, the only evidence I am aware of as to the appetite amongst employers for using the flexibilities to reduce tax and NI indicates that significant numbers of employers will do so.

28. I point specifically to two pieces of research—one by my own magazine, Corporate Adviser, and one by Jelf Employee Benefits, a pension and benefits consultancy.

29. In a poll of 39 of the UK’s leading DC pensions consultants, taken at the Corporate Adviser Summit in October 2014, two thirds said they predicted at least 10 per cent of the available NI and income tax that could be avoided by over-55s flushing cash through pensions rather than salary would be avoided, with 35 per cent thinking more than 20 per cent would be. More than half of those present expected at least some of the employers they advise to take advantage of the opportunities for tax and NI avoidance presented by the April 2015 changes in access to pension assets.

30. Corporate Adviser Summit Survey results:

Assuming £20bn or so of NI and income tax can be avoided by over-55s flushing cash through pension rather than salary in 2015/16, what proportion of that figure will be avoided?

<table>
<thead>
<tr>
<th>Percentage</th>
<th>Count</th>
</tr>
</thead>
<tbody>
<tr>
<td>None</td>
<td>0</td>
</tr>
<tr>
<td>0-10%</td>
<td>32</td>
</tr>
<tr>
<td>10-20%</td>
<td>26</td>
</tr>
<tr>
<td>20-30%</td>
<td>18</td>
</tr>
<tr>
<td>30-40%</td>
<td>11</td>
</tr>
<tr>
<td>40-50%</td>
<td>3</td>
</tr>
<tr>
<td>More than 50%</td>
<td>3</td>
</tr>
</tbody>
</table>
Do you expect any of your employer clients to flush more over-55s pay through pension rather than salary as a result of the freedom and choice in pensions changes?

1. Yes 53% 53%
2. No 47% 47%

A survey 192 employers with between 50 and 2,000 employees carried out by Jelf Employee Benefits found at half are looking to exploit tax advantages arising from the new pension freedoms. In the survey, which was carried out in July 2014, 35 per cent said they would offer all of their older workers greater remuneration flexibility so that they can benefit from the new freedoms, while 15 per cent said they would consider doing so for some employers on a case-by-case basis. Only 6 per cent said they would not offer this option, with 44 per cent undecided.

It is clear some employers intend to use the new flexibilities to reduce tax and NI. The Treasury appears to be saying it will allow this to happen until losses are significant. However, if and when the Treasury does decide to clamp down on abuse, is not clear what abuse is or how it can tighten the rules without affecting existing pension provision that has been set up in good faith under the current outgoing rules. Employers currently have no idea what is permissible under the rules and what is not. But relying on both employers and employees not to take advantage of significant tax and NI savings seems foolhardy.

It is worth highlighting to the Committee the suspicion I have that the Government had not spotted the potential loss of NI and tax through increased salary sacrifice through pensions at the time the Budget was published. The pension flexibilities are extremely popular with the public, and restricting them would reduce that popularity. It is possible that Government reluctance to rein in the flexibility of a popular policy is outweighing its need to protect the public purse. My exchanges with the Government on the scale of the potential loophole, and its likely uptake, as set out below, suggest it was not aware of the problem.

Pensions minister Steve Webb told the Pension Schemes Bill committee that within days of the 2014 Budget “Paul Lewis of Moneybox was highlighting exactly the potential for cycling money around in this kind of way”. I have contacted Paul Lewis and he has confirmed he did not look at NI loss through salary sacrifice at all—he just looked at tax loss. In the scenarios I have laid out, the loss to the Treasury of NI is five times bigger than the loss of income tax for basic rate taxpayers. Paul Lewis’s account would appear to contradict the minister’s submission to the Committee that this is something the Treasury and DWP have known about all along. This view is reinforced by the fact I have made repeated requests of Treasury and DWP for details of their assessment of the potential NI loss since May 2014 and have still received no substantive response.

The Government’s approach seems to be leaving many billions of pounds worth of tax and NI relief on the table and hoping take-up of it will be minimal. The only thing stopping advisers and employers from establishing structures to maximise this loophole is the threat that if they do so in large numbers, they will be stopped from doing so.

**Detailed example**—how salary sacrifice cuts the Treasury’s tax take

An employee aged 55 or older is paid £40,000 a year.

If the entire sum is paid as salary, the individual pays employee Class 1 NI Contributions at 12% for earnings above the primary threshold of £7,956, totalling £3,845.28.

He also pays 20% income tax on earnings above the £10,000 personal allowance, totalling £6,000.

Total tax paid by individual = £9,845.28

Total post-tax income = £30,154.72

AND His employer also pays employer NI contributions of 13.8% for earnings above the primary threshold of £7,956, totalling £4,422.07.

Total tax paid to HM Revenue & Customs = £14,267.35

If the individual opts to receive just the minimum wage as salary (£11,484.20 assuming a 35-hour week), and gets the balance of £28,515.80 paid into a pension, no employer or employee NI is due.

From April 2015 the entire pension can be drawn immediately.

**Tax on salary**

The individual pays employee Class 1 NI Contributions at 12% for earnings above the primary threshold of £7,956, totalling £423.38.
20% income tax is due on earnings above the £10,000 personal allowance, totalling £296.84.

Total tax on salary £717.22

Plus the employer has to pay NI of 13.8% on earnings above the primary threshold of £7,956, totalling £486.89

Tax on pension

The individual receives 25% of £28,515.80 as a tax free lump sum = £7,128.95

The remaining £21,386.85 is liable for income tax at 20% = £4,277.37

Total tax paid = £4,997.59

Total post-tax income = £35,005.41

Total tax paid to HM Revenue & Customs (incl employer NI) = £5,484.48

Loss to HMRC through freedom and choice in pensions = £8,782.87 (62% of its revenue when paid through salary)

November 2014

Written evidence submitted by Hargreaves Lansdown (TP 11)

SUMMARY

1. The changes being introduced via the Pensions Schemes Bill and the Taxation of Pensions Bill are welcome reforms however they come with significant risks. The pace with which they are being introduced means there is no proper overarching framework, nor is there sufficient time to address the myriad of unintended consequences.

2. We have set out below our principle concerns regarding the new freedoms.

   — Pensions by default: a government policy mismatch
   — Risks to investors
   — The role of regulated advice
   — The Guidance Guarantee
   — Market competition
   — Pension fraud
   — Behavioural responses
   — Hargreaves Lansdown proposals

3. In addition, we have made four suggestions more narrowly focussed on the Taxation of Pensions Bill itself.

   — Make the temporary extension of the block transfer definition permanent.
   — Only require an individual who has flexibly accessed pension benefits to inform the pension schemes of which they are an active member, rather than to inform all their pension schemes.
   — Allow the open market to be used for inherited drawdown and make it compulsory for the original provider to offer this option.
   — Allow drawdown payments for long term care to be tax-free.

PENSIONS BY DEFAULT: A GOVERNMENT POLICY MIS-MATCH

4. Auto-enrolment has undoubtedly been a very positive policy measure. It has rightly enjoyed cross-party support. Auto-enrolment is based on inertia. Members are defaulted into pensions, given a default investment, a default contribution rate and can therefore be defaulted all the way through the savings journey. This works up to a point, however in the context of the budget reforms it now means millions of pension members may arrive in their 50s with no familiarity with managing investments (see below). They will be expected to make complex decisions regarding their pension pot and other assets. The Budget freedoms have moved engagement from being desirable to being an absolute necessity.

RISKS TO INVESTORS

5. Briefly, we see the following risks as most likely to cause investor detriment, we can explore these risks in more detail if required:

   — Investment loss
   — Longevity underestimation
   — Longevity overestimation
Market return sequencing

Guarantee costs

Lack of regulatory accountability

Investment loss

6. An unexpected fall in capital or income could cause serious hardship.

Longevity underestimation

7. Investors typically underestimate their life expectancy by several years. Even if they have an accurate assessment of average life expectancy for someone with their characteristics, many will still exceed that average.

Longevity overestimation

8. The converse is also potentially a problem; investors could lead an unnecessarily frugal retirement and die with too much money in the bank.

Market sequencing risk

9. This is a critical but poorly understood risk. If an investor starts drawing an income from a fund and suffers a few early years of poor returns, they will irreparably damage their savings. By contrast, if they are fortunate enough to enjoy an initial few years of good returns, they may then be set for life.

Guarantee costs

10. You can ‘insure’ a pension fund to protect it from investment losses. These can be expensive and sometimes unreliable. Typically it costs around an additional 1% a year, just for the guarantee; this is more than the total price cap for all the costs involved in running a workplace auto-enrolment pension scheme (set at 0.75%).

Lack of regulatory accountability

11. If it does go wrong (and for some people, it will) there are at present no clear lines of regulatory accountability. Where will the buck stop?

THE ROLE OF REGULATED ADVICE

12. Where investors receive regulated advice, it is reasonable to assume they will get a good outcome. Whilst some advice in the past has been less than perfect and there have been miss-selling scandals, because the advice is regulated, investors will at least have some redress if serious financial detriment can be proved to have been caused by their advice. This is not a perfect system and availability of advice is limited and can be expensive. Typically advice costs hundreds of pounds to deliver. Many investors reaching retirement are unlikely to receive regulated financial advice until more cost-effective propositions are developed.

13. Investors will therefore be dependent on their pension provider for the retirement income solutions with which they are presented.

14. Pension providers generally, including insurance companies and trust based occupational pension schemes, have a poor track record of serving their customers and members well at retirement. In spite of repeated calls to the government and the FCA for reform of the retirement process, for years the Open Market Option has failed to deliver good outcomes for investors. Take up rates have been stuck below 50%. This means the majority of retiring investors have been buying a ‘suboptimal’ retirement income. The scale of loss is substantial too, with the typical spread of annuity rates between the best and the worst in the market running at between 20% and 40%.

15. Given this experience, it would be naïve to expect anything to change with the introduction of the new freedoms next year. The new freedoms do not of themselves do anything to promote better shopping around on the part of scheme members, nor do they ensure members will be offered market competitive solutions at retirement.

THE GUIDANCE GUARANTEE

16. The Government has promised all investors will be offered free, impartial, face to face guidance. This is not going to solve the problem. The Guidance is analogous to a seatbelt in a car; it is undoubtedly going to make the vehicle occupant safer, but is not a complete solution to road safety. The wearing of the Guidance ‘seatbelt’ is optional, and even with the Guidance, you still need the financial equivalent of airbags, a driving test, crash-testing, a highway code and a highway patrol.

17. Many investors will not take up the Guidance although it is hard to predict exactly how many, as there are still many unknown factors. One study resulted in just a 2.5% take up, though this should not be interpreted as a definitive guide to what may happen next year: The nature of the pre-retirement communications, the
publicity surrounding the Guidance, the ease of accessibility etc. will all make a difference. It is however safe to assume a significant proportion, quite possibly a majority, will not take up the Guidance. Even those who do receive the Guidance will still need to subsequently engage with commercial retirement income providers. This could be their existing pension provider, a drawdown provider or an annuity company.

18. When those investors do engage with retirement income solutions, there are at present very few safeguards to maximise the chances that the investor will get a good outcome. Pension providers’ past form (including Trust based schemes) indicate they will gravitate not to solutions which are best for their customers but to whatever is either simplest to administer or likely to generate the maximum profits.

19. An investor could simply contact their occupational pension scheme and ask for some money. From a regulatory point of view, all the scheme needs to do is send the money. Even if they are required to flag up the tax implications, there are no controls to ensure the investor is in a suitable investment fund, is drawing income at a sustainable rate, isn’t cashing in investments which have just fallen in value, or indeed will get a nasty shock when one day the money runs out. Critically, there are no regulatory mechanisms in place to hold those pension providers to account. Similarly, if the investor decides they want to buy an annuity there is no requirement for their pension provider or scheme to provide a competitive and suitable annuity.

**Market competition**

20. Nothing in the new reforms will increase the likelihood of market competition working to the benefit of the investor or drive any kind of shopping around process. Arguably it will be even easier for a pension provider to sell to an existing customer a poorly priced or uncompetitive product. They will not be subject to any regulatory controls on the sales process, or any scrutiny regarding their product pricing. Worst of all will be where an investor draws an income from an investment fund in a trust based scheme. In this case there won’t even be any product sale to regulate, so how can the regulator hope to supervise such transactions to ensure members are protected?

**Pension fraud**

21. It will be much easier to defraud the unwary now you don’t even need to set up a spurious pension scheme. All the fraudsters need to do is to target investors over the age of 55 and persuade them to unlock their pensions. The fraudsters will do this by promising plausible but slightly over-inflated ‘guaranteed’ investment returns from ‘special’ schemes. Anyone foolish enough to be drawn into such schemes will cash in their pensions, incur a tax liability, hand their cash over to an unregulated scheme and never see the money again. The risk lies in the unregulated market, so it makes sense to create a more distinct brand around the regulated advisers and investment schemes. We have proposed a solution below.

**Behavioural responses**

22. It is difficult to anticipate what consumer responses will be to these changes. We know from client research that whilst the new freedoms are very popular, many investors still want a secure income in retirement. In a survey of over 1,000 investors, 94% said a secure income was quite or very important to them.

**Hargreaves Lansdown proposals**

*Addressing market issues*

23. Hargreaves Lansdown proposes that any organisation arranging a retirement income for a pension investor has to accept some responsibility for that arrangement. This means ensuring:

- it is market competitive,
- the investor is offered suitable choices, and
- risks are clearly explained and suitable for the target market.

For example, investors who have remained disengaged throughout the accumulation stage of their pension probably shouldn’t be defaulted into market-risk based arrangements for the decumulation phase.

24. If the pension provider is selecting an investment strategy and level of income on behalf of the investor, then it is imperative the investor is left in no doubt as to the level of risk they are facing, in terms of loss of capital and/or income and the extent to which they will be protected from such consequences.

25. If the investor is being protected through the use of hedging or derivative strategies to insure the fund or income against loss, then the investor needs to know the cost of that protection and the possible impact on investment returns (which can be considerable).

26. The formulation of a suitable regulatory structure to protect the vulnerable, to drive up standards and to promote market competition in the retirement income market is a complex challenge which needs to be completed in a very short time. A close watch needs to be kept on the development of this market, both in terms of the pensions industry’s answers to the challenges and also the FCA’s and The Pensions Regulator’s regulatory responses.
27. The risk of pension fraud means a clear distinction needs to be drawn between regulated and unregulated investments and advisers. There should be a clear Kitemark or logo which is only available for use by regulated businesses. It should also be an offence for any unregulated business to use this logo. This would then allow regulators, the media and the industry to promote a very clear message to investors: don’t do business with unregulated entities; if you do and you lose your money, you’ll have no come-back.

Making the temporary extension of the block transfer definition permanent

28. Some individuals have an historic right to take pension benefits before normal minimum pension age and/or a right to greater tax-free cash then the standard 25%. If these individuals wish to retain this protection there are restrictions on how they can transfer between pension schemes. The main restriction is that any transfer must involve at least one other member of their pension scheme.

29. When the pension freedoms were announced it was recognised that the only way these individuals would realistically be able to use these freedoms were if the new options were offered within their existing pension scheme. The Finance Act 2014 therefore temporarily extended the definition of a block transfer to allow these individuals to transfer without another member and still retain this protection.

30. Once this temporary extension expires many individuals who do not want to lose this protection will again be effectively trapped in their existing pension scheme and unable to use the pension freedoms. We therefore suggest that this temporary extension is made permanent by omitting sub-paragraphs (b) and (c) from Finance Act 2004, Schedule 36 paragraph 22(6A).

Information requirements for individuals who have flexibly accessed pension

31. Paragraph 87 of the schedule adds to the existing information requirements.27 This requires an individual to inform all pension schemes of which they are a member when they have first flexibly accessed pension benefits or the first time a drawdown pension fund becomes a flexi-access drawdown pension fund.28

32. Given that the average individual could have eleven pension schemes in their lifetime and the estimated £400 million of unclaimed money which is in pension and life assurance schemes this is a disproportionate requirement which is unlikely to be fully met. We therefore suggest new regulations 14ZB and 14ZE are amended so the information requirement will only apply to schemes of which the individual is an active member or to which they pay a relevant contribution. This could be achieved by using similar wording to that used in paragraph (1) of new regulation 14ZD.

Inherited drawdown—using the open market

33. Current legislation only allows for dependant’s drawdown if it is offered by the pension scheme of the deceased member. The proposed amendment to the Taxation of Bill also specifies that dependants, nominee or successor income drawdown will only be available when designated under the pension scheme of the deceased member.

34. Within the Treasury document published on 1 October 2014 it states, in relation to beneficiary’s drawdown, that The Government is aware that in some cases, a pension provider may choose not to offer drawdown. In addition, the National Association of Pension Funds’ written evidence submitted to the Pension Schemes Bill committee states that schemes and their service providers cannot make expensive system changes without the certainty of Royal Assent and made regulations. It seems clear that for many individuals, beneficiary’s drawdown will not be available from 6 April 2015.

35. We therefore suggest that where a pension scheme is not yet ready to offer beneficiary’s income drawdown they should be required to offer an option whereby the fund is designated as available for beneficiary’s income drawdown immediately before being transferred to a pension scheme which is able to offer full beneficiary’s income drawdown.

Drawdown payments for long term care to be tax-free

36. In April 2015 both part one of the Care Act 2014 and the Taxation of Pensions Bill are due to be implemented. This provides the opportunity for joined-up legislation covering both pensions and long term care. In particular, this allows pension funds to be used to fund long term care.

37. The reasoning behind incentivising retirement saving also applies to incentivising long term care saving. This could be achieved by a specialist savings vehicle providing incentives to contribute, restrictions on early withdrawal and incentives not to withdraw savings. This would however take time and money to set up even before any individual started to build up any savings.

27 The Registered Pension Schemes (Provision of Information) Regulations 2006 (SI2006/567)
28 New regulation 14ZB
29 New Regulation 14ZE
30 DWP—Making Automatic Enrolment Work p11
31 Experian Unclaimed Asset Register website, retrieved on 6 November 2014
32 Finance Act 2004, schedule 28, paragraph 22
33 Finance Act 2004 section 167(1A) as to be inserted by New Schedule one to the Taxation of Pensions Bill
38. A pension already provides for tax relief on contributions, is broadly free of tax while invested and has a minimum age at which pension investments can be withdrawn. The provision in this Bill to allow pension assets to be passed down free of tax on death before 75 will also remove an incentive to remove money from pensions between minimum pension age and 75.

39. The one shortfall preventing a pension from being a vehicle which would be used to fund long term care is the lack of an incentive to retain monies within a pension after 75. To rectify this shortfall it should be made more cost effective to fund long term care from within a pension than from outside a pension.

40. We therefore suggest that payments from a pension to a registered long term care provider for the benefit of the individual or their spouse/partner should be free of income tax. This would mirror the way in which a non-pension immediate care annuity can be used to pay for long term care.

ABOUT HARGREAVES LANSDOWN

Hargreaves Lansdown is a leading provider of investment management products and services to private investors in the UK.

Hargreaves Lansdown is a diversified business with an established reputation for providing the best information, service and value for money investments and products to private and corporate investors.

The HL Vantage Service is the largest direct to consumer investment and pension supermarket in the UK and the only Which? Recommended Provider.

Hargreaves Lansdown administers over £44.3 billion of client assets through the Vantage Service directly on behalf of over 662,000 investors. In total, Hargreaves Lansdown has £47 billion of assets under administration and management (30 September 2014).

Founded in 1981 by Peter Hargreaves and Stephen Lansdown, Hargreaves Lansdown floated on the UK stock market in May 2007 and is currently listed in the FTSE 100.

For more information www.hl.co.uk/about-us

New ISA: www.hl.co.uk/nisa
SIPP: www.hl.co.uk/pensions/sipp
Annuities: www.hl.co.uk/pensions/annuities
Drawdown: www.hl.co.uk/pensions/income-drawdown
Vantage Investment Platform: www.hl.co.uk/vantage

November 2014

Written evidence submitted by the Association of Taxation Technicians (TP 12)

1. INTRODUCTION

1.1 The Association of Taxation Technicians (ATT) is pleased to have the opportunity to comment on the draft legislation ‘Taxation of Pensions Bill’.

1.2 We have limited our comments to the proposed new reporting requirements which are set out in Part 6 of the Bill and also referred to in Chapter 8 the draft guidance released by HMRC on 21 October 2014. Pages 38 to 46 of this guidance cover reporting requirement that are already included in the draft Bill and also those which are still to be provided for in secondary legislation.

2. OUR COMMENTS

2.1 Onus on members to report to other scheme administrators

Sections 8.1 to 8.3 of the draft guidance outline the procedure for notifying all schemes (of which an individual is a member) when that member has flexibly accessed their pension fund.

These provisions seem to put a lot of the burden onto a member to inform all of the other scheme administrators and specify a deadline of just 31 days to do so.

The scheme administrator of the fund which was first flexibly accessed has 31 days to inform the member of the obligation to inform their other scheme administrators. This is a fair time period as it will involve just one correspondence to that member and that should be achievable within the 31 day period.

However, we believe it is a very short deadline for the member to then have to contact all of their other schemes and we believe that the deadline for the member to do this ought to be extended to, say, 45 or 60 days, to recognise that there may be a number of letters or telephone calls that the member will need to undertake.
We also believe that the introduction of these new rules should be preceded by a well-publicised educational and promotional campaign put in place so that members understand their obligations and are not left bewildered by the terminology. For example, the requirement for a member to inform a scheme when they have flexibly accessed their pension for the first time will not apply if the individual became a scheme member as a result of a recognised transfer. It may be perfectly obvious to a pension advisor or other professional when this exception applies but the member may not be quite as well informed and so they will need to have adequate support and assistance to help them know who they do and do not need to inform.

2.2 Penalties

The issues discussed in section 2.1 above become all the more important to consider as section 8.9 of the draft guidance indicates that penalties will be charged if the information is not provided on time. These penalties will be levied on the person who should have provided the information.

The whole idea of pension flexibility is such a new concept and the raft of new regulations being introduced in the Taxations of Pensions Bill will take time to be absorbed by everyone involved. In addition, final legislation is only likely to be published shortly before the implementation date of 6 April 2015. Taking all of this into consideration, the ATT believes that there is a case for the charging of penalties to be phased in gradually (as was the case with Real Time Information reporting) rather than imposing a penalty regime immediately from 6 April 2015 when everyone, members especially, are still getting to grips with the whole of this new regime.

2.3 Real Time Information (RTI)

When the ATT responded to the initial consultation Freedom and Choice In Pensions, we specifically highlighted that our major area of concern was the impact the reforms to the pension tax framework would have on PAYE systems. We commented:

‘If the taxpayer has the ability to draw down from more than one fund in a tax year, how will HMRC be able to apply the correct tax codes so that the correct amount of tax is collected in the year? A system that allows full flexibility is likely to lead to many more tax positions needing to be reconciled after the year end. Does HMRC have enough resources to cope with this on a timely basis?’

Section 8.10 of the draft guidance says nothing that alleviates our concerns in this area. In fact HMRC appears to be relying on end-of-year reconciliations in the vast majority of cases in order to rectify tax positions. It appears from the guidance that HMRC believes (and accepts) that only in cases where there is more than one payment (either regular or irregular) will there be no need to reconcile a person’s position at the year end. However, this is only true if the payments come from the same pension fund and the member has taken no other payments from any other pension fund in the same tax year.

HMRC has advised that the emergency code will not be operated where a P45 or tax code is provided. The ATT believes that the number of instances where either document is provided or even available will be very few indeed. If a member takes a flexible pension drawdown payment and it is the first one they have taken then what code can be operated, other than an emergency tax code? The member may have a tax code from an earlier year but it would not be appropriate to operate this code in very many cases.

Consider the case of someone who currently has only a state pension or even a small regular annuity which amounts to less than the personal allowance. Previously, HMRC may have issued a tax code that was not operated because there was no liability. The tax code would have existed, though, and the member would have been able to provide this code to a scheme administrator in the event of taking a flexible pension drawdown. We still do not believe that the application of the code would enable the correct amount of tax to be deducted in the case where a one-off withdrawal is made but it would at least make the error in the tax collected less than it would be using the emergency tax code.

HMRC has said that, under proposals to change how PAYE tax codes are issued, where it considers there is no tax liability a tax code will no longer be issued. Therefore, in our example, when a flexible drawdown payment is taken there will be no code currently in issue, resulting in the emergency code having to be used and an almost certain larger overpayment or underpayment occurring. Will HMRC now reconsider this proposal to hold back PAYE tax codes where it considers no liability arises, as it cannot know, now more than ever, what further pension income a pensioner may take in the tax year and that code ought to be available to the pensioner?

We do wonder whether HMRC has considered the resources it will need to deal with the very many reconciliations it will have to deal with. HMRC has said in the draft guidance that it will look to make repayments in-year, where the RTI system is correctly noted to show that a scheme has ended. However, a repayment made in-year based on the information of that one scheme would not take into account the payments a member might receive from other schemes that may be using the emergency code or an incorrect tax code. So a reconciliation at the year-end would still be needed and the repayment made in-year may need to be repaid to HMRC.

We considered all along that HMRC would have issues in getting someone’s tax position correct during the year when there was complete flexibility over pension. However, simply sitting back and relying on end-of-year
reconciliations does not seem to be good enough, especially if the resources to deal with those reconciliations on a timely basis are not there.

Based on the proposals as they currently stand, it would appear to us that the only way a pensioner can be assured of having their tax affairs dealt with correctly would be to voluntarily complete a self-assessment tax return and claim any refund due through this recognised mechanism where returns can be dealt with electronically and refunds issued on a timely basis. As HMRC has, over the past few years, been keen to reduce the number of self-assessment tax return cases, surely it can only see an increase in the number of returns being submitted as undesirable. However, it seems highly unlikely that the ‘correct amount of tax’ will ever be deducted under PAYE with the proposed system and many taxpayers will face a frustrating wait to reclaim their money or indeed be faced with large tax liabilities coming out of the blue long after the tax year has ended—unless they voluntarily complete a self-assessment return.

The ATT has worked for a number of years with HMRC’s consultation group that deals with PAYE underpayments caused through HMRC error (ESC A19 cases) or employer error. We are concerned that any progress being made in this area will be curtailed by the increase in reconciliations created by these new proposals. Furthermore, we are concerned about the impact on ESC A19 cases since underpayment or overpayments being created during the year might start to be seen as the ‘norm’ (it certainly seems to be HMRC’s attitude from the reading of section 8.10). This might then erode the idea that any taxpayer could have a reasonable belief that their tax affairs were being dealt with correctly. There appear to be absolutely no assurances that tax affairs will be dealt with correctly for pensioners who take benefits under the new regime and it would seem they might have very little protection from ESC A19 as matters stand.

We note that the guidance says that the changes to RTI reporting are expected to be as they are currently set out in section 8.10 but are subject to change. We would urge HMRC to have a rethink about how best to deal with the collection of PAYE on flexible pension drawdowns before the secondary legislation is published. The PAYE system works satisfactorily in most cases of regular payments of salary or pension, but it would appear totally unable to get anywhere near the correct position for a one-off withdrawal. HMRC should consider whether there needs to be some entirely new basis for determining the initial tax deduction at source for a withdrawal from a pension fund as we believe that PAYE is unfit for purpose in this case.

3. SUMMARY

3.1 We have covered the main concerns we have regarding the draft Taxation of Pensions Bill, focusing on the reporting requirements covered in Part 6 of the Bill and as outlined in Chapter 8 of the draft guidance issued by HMRC on 21 October 2014.

The ATT remain deeply concerned about the impact on the income tax position of pensioners considering taking benefits under the new regime. A system based on many end-of-year reconciliations being carried out with no legislative framework or structure (such as there is, for example with the self-assessment system where assessments are appealable—P800s are currently not appealable) will only lead to chaos and misery for very many frustrated pensioners.

4. NOTE

4.1 The Association is a charity and the leading professional body for those providing UK tax compliance services. Our primary charitable objective is to promote education and the study of tax administration and practice. One of our key aims is to provide an appropriate qualification for individuals who undertake tax compliance work. Drawing on our members’ practical experience and knowledge, we contribute to consultations on the development of the UK tax system and seek to ensure that, for the general public, it is workable and as fair as possible.

Our members are qualified by examination and practical experience. They commit to the highest standards of professional conduct and ensure that their tax knowledge is constantly kept up to date. Members may be found in private practice, commerce and industry, government and academia.

The Association has over 7,500 members and Fellows together with over 5,000 students. Members and Fellows use the practising title of ‘Taxation Technician’ or ‘Taxation Technician (Fellow)’ and the designatory letters ‘ATT’ and ‘ATT (Fellow)’ respectively.

November 2014

Written evidence submitted by ABI (TP 13)

INTRODUCTION

1. The Bill legislates for the announcements made in the Budget 2014, to allow people aged 55 and above to access their pension savings as they wish, subject to their marginal rate of income tax. The new rules are planned to take effect from April 2015.
SUMMARY OF ABI POSITION

2. The industry strongly supports the reforms in principle. They should give people a greater sense of ownership of their pension pot and lead to more pension saving which is critical if people are to have a dignified retirement. They are also consistent with the direction of changes we had campaigned for: in particular, allowing access to higher lump sums (through changing trivial commutation and small pot rules), and greater flexibility for retirement products to adapt to paying for social care.

3. The objective of the reforms has to remain focused on giving people more choice in generating income from their retirement pots in a way which works for their personal circumstances—not simply to access their savings much earlier than when the vast majority of British workers plan to retire, which for most people would not be the right choice.

4. The industry supports the reforms, we want them to be a success and our members are working flat out to get everything ready for April 2015. However, although the tax position is becoming clearer, ongoing work on how the regulatory aspects of the new rules will work in practice, and on what the guidance for savers will look like, needs to be taken forward as a matter of extreme urgency. Government and regulators need to work together with the industry to ensure customers have access to flexibility with a level playing field between products and providers. We need certainty and no headline-driven announcements if our members are to be able to help make the reforms a success, all at the same time as helping employers automatically enrolling thousands of employees, implementing the charge cap and governance reforms, and taking part in a major legacy audit.

KEY ISSUES

Pension flexibility, not early access

5. Pension reform is about building assets for income in retirement for a much larger part of the population.

6. The Government has implemented a compulsory framework for employers, which is designed to create a savings culture for long term financial resilience in old age. Automatic enrolment has seen millions more people saving for their retirement and further pension reforms should build on this.

7. We are therefore very concerned that the focus of recent discussion on the Budget reforms has been about early access to cash at age 55 rather than on giving people more choice about how to use their pension savings to generate retirement income. At age 55, people may have 30 years of active life ahead of them including potentially significant care costs. For most people, depleting their pensions at the age of 55 will therefore be a poor decision that could easily lead to straitened circumstances later in retirement and reliance on the state for care costs. Narrowing down the debate to access to cash at age 55 also has the potential to deal a fatal blow to the Government’s wider reforms of encouraging people to work for longer, and making society more financially resilient—both critical if the UK is to navigate the challenges of an ageing population successfully.

8. This underlines that we need to refocus the debate on managing incomes in retirement and the choices and decisions people face from working age through to retirement.

Consumer information and advice

9. Giving customers more choice is welcome but it is also imperative to recognise that good guidance and advice is vital to prevent people making decisions which could lead to retirement poverty and / or to them giving up valuable benefits. Providers are therefore committed to ensuring that the new pension guidance service succeeds and is valuable to people considering their retirement options. The recent Government clarity that the Citizens Advice Bureau will provide face to face guidance and that telephone guidance will be provided by The Pensions Advisory Service is a step forward.

10. However, not all savers will take up the guidance, and the potential for scammers to become active in this market is clear. With the take up of guidance uncertain, it is essential that the Financial Conduct Authority (FCA) develops appropriate safeguards in time for next April. We believe it is essential that providers of all retirement products should highlight risks to consumers in a consistent way, and would like the FCA to clarify what providers are able to say when interacting with their customers. Equally, all of us including Government and regulators should intensify our efforts to guard against fraudulent activity.

11. Many people will struggle to understand the tax consequences of these reforms. Apart from tax free lump sums, withdrawals from pension pots are taxable pension income and this may not be fully understood. Not only may people find themselves unexpectedly paying higher rate tax, it is possible that some will be unaware that their tax may not be settled for a year after they have accessed their funds through a self-assessment process that they may be unfamiliar with. Again, this shows the need for the guidance service to be high quality and effective, highlighting the tax consequences of pension withdrawals, and for the FCA to be clear about its expectations of providers where customers do not take up the guidance.

Tax and regulation: need for clarity and level playing field

12. The regulatory rules affecting a number of key changes in the Bill are not yet clear. We are discussing these points with the Government and the FCA, but without urgent clarity there is a risk of some customers not being able to access flexibility and of an uncertain environment and uneven playing field between different types
of product and providers. This is not solely the role of the FCA—it requires coherent and achievable measures from the Treasury, HMRC, the Department for Work and Pensions, the FCA and the Pensions Regulator.

13. For instance, the FCA is urgently considering the regulatory position around accessing a pension pot in one lump sum—whether through Flexi-Access Drawdown or an Uncrystallised Funds Pension Lump Sum—but the longer this remains unclear, the more difficult it is for providers to plan and develop requisite systems. This is despite that taking a pension pot in this way was a key expectation raised as a result of the Budget reforms. Similarly, the whole regulatory regime around the Uncrystallised Funds Pension Lump Sum route which forms the basis of the Government’s ‘pension bank account’ analogy has yet to be resolved. In addition, there could be gaps in regulation between contract-based and trust-based schemes in two key areas. Firstly, how drawdown in trust-based schemes will be regulated; secondly, protection for customers and expectations of providers, if a customer wants to transfer out of a defined benefit scheme after receiving advice not to do so.

14. Providers welcome the sensible reduction of the 55% tax charge on death, which the ABI had previously asked the Government to consider. The 55% tax charge had stood in opposition to the wider Government policy of making pension saving more popular by giving people more options on how to use their retirement savings. However, without further clarification it creates an advantage for drawdown customers over annuity customers, which will change behaviour. To ensure that the policy is not skewed against income, tax on pension payments to a beneficiary after the customer’s death should be treated equally, whether paid through an annuity or drawdown, as income or as a lump sum.

Product innovation

15. Providers will respond positively to the 2014 Budget reforms as the new rules should allow for better product solutions to be offered to cope with historically low levels of interest rates and high levels of longevity in retirement. There are already annuities with potential for growth, and drawdown with guarantees, and we can expect new variations on these.

16. Two changes to the Bill would enable providers to make further use of flexibility:

— Extending the maximum period for a short-term annuity in a drawdown contract from five years, which is unnecessarily restrictive, to a much longer period such as 25 years. This would allow customers to access a guaranteed income for longer, potentially at higher rates, while benefiting from the flexibility of drawdown.

— Allowing existing capped drawdown customers to designate further funds to capped drawdown arrangements within the same scheme. At present, the Bill only allows further designation to the same capped drawdown “arrangement”, but this could inadvertently rule out some customers from continuing in capped drawdown.

17. However, the regulatory regime and the tax framework will be critical to the degree of innovation possible in the post-April 2015 market. Both conduct and prudential regulators will need to take sensible and proportionate approaches to the sale of new products and the capital required behind them, if the Government’s ambitions for an innovative market are to be fully met.

Measures to remove tax advantages

18. The changes to the retirement tax framework could have created significant opportunities for individuals taking unfair tax advantages. The Bill implements sensible and welcome measures to prevent this, which the ABI strongly endorses. Once an individual has made use of the new flexibilities, for example drawn down more than their tax-free lump sum, they will still benefit from tax-incentivised pension saving, but their annual allowance will be reduced to £10,000. This makes it clear that people cannot exploit the Budget reforms by using them for tax planning purposes through avoiding tax on earnings. At the same time, it ensures that individuals can safely access an existing pension pot flexibly (such as due to redundancy or ill health, or because they want to support their children) but still save into a pension later.

19. Reducing the annual allowance for savers who have accessed flexibility goes with the grain of consumers’ current understanding of how the system works and does not expose consumers engaged in normal saving behaviours to the risk of inadvertently being caught by rules designed to prevent tax avoidance.

Social care

20. When the Budget reforms were announced, the Government was clear that the flexibility created was an opportunity for product providers to create solutions for older people who wanted to make provision for their care needs.

21. The ABI signed a Statement of Intent with the Department of Health in January 2014 demonstrating the willingness of providers to be part of society’s response to the challenge. Of equal importance is the need to develop the demand for care products through a government led public awareness campaign and we are pleased that the Department of Health is taking this forward. A well informed and active market for care will enable providers to develop and grow the market for long term care products.
22. However, we are concerned that a continued focus on early access at the age of 55 means that there may be barely enough in the pension pots of some savers to cover their near-term retirement income needs, let alone enough left to stretch to care costs in older age.

Investment in infrastructure

23. The insurance industry plays an essential part in the UK’s economic strength, managing investments of £1.8 trillion—equivalent to 25% of the UK’s net worth. If the momentum towards early access continues, the prospect of the pension sector providing long term investment fuel for economic growth is reduced. Pension providers, whether trust based occupational schemes, contract based schemes, or retirement income providers, will face greater requirements to be ‘liquid’ from age 55.

24. The long-term nature of annuity books helps the insurers who run them to invest in the UK economy, especially in long-term projects like infrastructure. If pensioners take more of these assets at the point of retirement and keep them in a bank account or invest in other assets (such as buy-to-let), the long term investment effects for the UK economy from the insurance sector over time may be significant.

November 2014

Written evidence submitted by National Association of Pension Funds (NAPF) (TP 14)

OVERVIEW OF NAPF RESPONSE

INTRODUCTION

The National Association of Pension Funds (NAPF) is the voice of workplace pensions in the UK. We speak for over 1,300 pension schemes that provide pensions for over 17 million people and have over £900 billion of assets. We also have 400 members from businesses supporting the pensions sector.

We aim to help everyone get more out of their retirement savings. To do this we promote policies that add value for savers, challenge regulation where it adds more cost than benefit and spread best practice among our members.

GENERAL COMMENTS

This Bill is an important part of delivering Freedom and Choice. Our primary concern is that the required structures and frameworks to enable schemes to begin to build Freedom and Choice capability for savers are in place well in time for April 2015. The timeline for implementation is very tight, and the Government needs to focus urgently on the delivery and implementation of the provisions of both this Bill and the Pension Schemes Bill.

Across the Freedom and Choice agenda there remain a large number of issues on which schemes require urgent clarity and which Government needs to address well before next April. We have included as Appendix 1 a list of “known unknowns” that summarise the questions that remain to be resolved in order for the full range of freedoms to be available to members of defined contribution (DC) schemes and for the implementation of Better Workplace Pensions to take place. A number of these will be resolved once this Bill gains Royal Assent, though the vast majority depend on the passing of the Pension Schemes Bill through Parliament and subsequent regulations.

In order for the wider reforms to the pensions landscape to be successful, it is essential that schemes are able to communicate the new and often complex options clearly and simply to savers. Concepts like “crystallisation” will be important to understand when the new freedoms come into effect, yet they will be difficult to convey and are poorly understood by the average saver. We encourage the Treasury and providers of the Guidance Guarantee to work with our members to develop simple ways of communicating the available options to members.

PROVISION FOR PENSION FLEXIBILITY

We support savers being given greater freedom and choice over what to do with their pension savings at retirement. However, in an environment in which savers are able to choose from a wider range of options at retirement than ever before, the need for them to be supported in making a decision has never been clearer. According to our 2014 Workplace Pension Survey, only 19% of savers feel very confident in knowing what to do with their savings even now, with only 14% of respondents saying they will not need any guidance whatsoever.

Individual confusion and bewilderment stands to increase significantly in an environment of greater freedom and choice.

Next April will be a particularly confusing time for those retiring, particularly as they may find that certain freedoms and options that they have heard about may not be offered by their particular scheme, which may not by then have developed the systems to deliver the full range of freedoms. Additionally, some new products

34 NAPF Workplace Pension Survey, 2014
on the market may carry costs and risks that are not immediately clear to consumers and some may only be accessible through a financial adviser, which could carry costs that many individuals will be unable or unwilling to meet. Fewer than half (43%) of respondents to our Workplace Pension Survey indicated that they were willing to pay anything towards financial advice, with only 3% willing to pay more than £300. Recent research has indicated that advice on converting a £100,000 pension fund into a lump sum and annuity would cost a median of £1,500, with advice on a £200 per month pension contribution at a median cost of £500.35

Even with the help of Guidance, some savers may be unable or unwilling to make a decision, and it is important that they still have access to decent retirement outcomes. Pension schemes can potentially help their members decide how best to access their retirement savings by using their expertise to highlight options that offer good value for money and have high standards of governance, communication, investment and risk management. This is a development that should be encouraged by Government within schemes that have robust governance arrangements that ensure they are acting in their members’ best interests. Trustees should be able to direct and support their members in this way without being deemed to have given advice.

**Drawdown pensions and pension payments out of uncrystallised funds**

Given the late arrival of legislative certainty, we expect few trust-based schemes to be able to offer either flexi-access drawdown or uncrystallised funds pension lump sums (UFPLS) by April 2015.

Savers who want to access flexi-access drawdown or partial UFPLS but cannot do so through their existing schemes will need to turn to the retail market and transfer their funds. The market in mass market drawdown products is itself not yet developed and savers may face a significant premium on charges in default accumulation funds, through higher charges and advice costs. The ongoing costs to savers could prove excessive for those with modest pots and, while some Mastertrusts may eventually offer new lower cost drawdown solutions, it is not yet clear that trustees of other schemes can direct their members towards them, or how members will be able to gain access to these solutions on the open market.

We are concerned that there is a gap between what has been promised by the Government and the media in terms of Freedom and Choice—for example, that savers will be able to access their pensions “like a bank account” from April 2015—and what will actually be available to retirees in April. This may prove confusing and frustrating for savers, many of whom may revert to choosing either the easiest or most heavily-promoted option, which may not deliver the best outcomes. The Government must be careful not to fuel media expectation and frustration among savers for certainty over flexibility.36 82% of respondents in our Understanding Retirement research stated that they wanted their pension to provide them with a regular income throughout their retirement, with a majority (55%) of respondents to our Workplace Pension Survey saying they would accept a lower return on investment in exchange for a guaranteed minimum income level. Even looking at the Guidance Guarantee, our research indicates that most people will be looking for it to provide an understanding of how to secure a regular income throughout retirement.

However, the annuities market has not been working well for consumers. Despite awareness of the right to shop around under the Open Market Option (OMO), savers often do not do so and end up selecting an annuity from their existing provider, often losing out on extra income in retirement. FCA research into the annuities market showed that around 150,000 savers could have got a better deal in 2013 had they not stayed with their existing provider, identifying consumer detriment in excess of £200 million—yet progress in reforming this market appears to have stalled. We look forward the completion of the FCA’s competition review of the annuities and wider retirement income market, which must ensure this important sector works well and delivers good value for all savers by April 2015.

**Annual allowances**

We welcome the pragmatic approach the Bill has taken towards mitigating the risks of widespread tax avoidance. In order for costs and burdens and schemes to be limited as much as possible, the implementation of the new annual allowances must be kept as simple as possible for schemes and for savers. It will therefore be important that HMRC both keeps reporting requirements simple, with schemes able to assume the £40,000 annual allowance is in place unless informed otherwise and only requires tax charges to be paid via the scheme when related to the £40,000 annual allowance, not the reduced allowances.

The application of the new annual allowance rules will be very complicated for those running hybrid pension schemes, and could affect some scheme members making legitimate contributions. We are skeptical that hybrid pension schemes will be abused for tax avoidance purposes. We believe it would be both fairer and simpler

36 NAPF Understanding Retirement research series, 2014
for a charge to be triggered on the higher defined benefit (DB) or defined contribution (DC) amount, with the more stringent rules outlined in the Bill only implemented if evidence emerges after April 2015 that new hybrid schemes are actually being set up for the purposes of tax avoidance.

We broadly support measures designed to bring more clarity to savers, particularly in an environment of greater freedom and choice. However, we are concerned that the requirement for savers to notify all of their schemes of having accessed their pension flexibly within 31 days is a heavy administrative burden to place on individual savers, many of whom lack awareness and confidence when it comes to managing their savings even now.

November 2014

Supplementary written evidence submitted by National Association of Pension Funds (TP 15)

APRIL 2015 PENSION REFORMS: 100 KNOWN UNKNOWNS

This document summarises the questions and uncertainties that remain to be resolved (as at October 2014) in order for the full range of new pension freedoms to be made available to members of DC pension schemes and for the implementation of Better Workplace Pensions to take place. Some of these questions set out in this document have been partially answered by command papers, draft regulations, and legislation that is being considered by Parliament. However the questions cannot be considered to be fully answered until the legislation receives Royal Assent and regulations are made, as schemes and their service providers cannot make expensive system changes without that certainty. The unknowns fall into the following main categories:

FREEDOM & CHOICE

Reduced Money Purchase Annual Allowance

1. Have structures been put in place at HMRC to detect members who exceed their annual allowance?
2. How will the reduced allowance affect beneficiaries who inherit a member’s flexi-access fund and take drawdown from it, if at all? Will it vary according to whether or not the individual takes an income? Will this differ according to the member’s age at death?

Taxation of benefits on death

3. Will dependants receiving income as a result of annuity guarantee periods be allowed to take these funds as lump sums once again? How will such lump sums be taxed?
4. Is the before/after age 75 distinction likely to remain?
5. Why is it OK for those taking drawdown from inherited funds to not be taxed (if death before 75) but beneficiaries who choose to buy an annuity to have to pay marginal rate of tax?
6. When will schemes have to move from the 45% tax rate to marginal rate on payments to beneficiaries?

Some answers expected in amendments to Taxation of Pensions Bill currently before Parliament.

COMMUNICATION WITH MEMBERS (DISCLOSURE)

7. What changes will be made to annual statements? For example, will CETV estimates be required for DB?
8. Will schemes still have to do projections of fund value / income in retirement at all and particularly when member in drawdown?
9. What changes will be made to wake-up letter and other OMO-related communications requirements?
10. Will there continue to be different open market option procedures for contract-based and trust-based schemes?
11. How will trustees be required to signpost members regarding the availability of the guidance guarantee?
12. Which points in time will be relevant for trustee signposting, given that decisions for DC members about how they are likely to want to take their benefits will start affecting their investment strategies as they get into their 50s?
13. Will AVCs on DB and funded public sector schemes be covered by the same disclosure requirements as DC schemes?
14. How will schemes be required to notify members of:
   — the requirement for advice on transfer from DB to DC?
   — the reduction in the annual allowance where they have taken flexi-access funds?
— The tax and benefit implications of taking their pension as a lump sum?

**Some answers expected in secondary regulations laid before Parliament in early 2015. Some issues awaiting FRC review of annual statements? Some issues may require new guidance from TPR.**

**Transfers**

15. Will any changes be made to members’ rights to transfer from a DC scheme, in order to facilitate freedom and choice?

16. Will there be any changes to the way that cash equivalent transfer values are required to be calculated as a result of the new legislation?

17. How will the right to transfer work where the scheme operates an underpin and the benefit may be either DC or DB on date of retirement, depending on how well the investments have performed?

18. How will the new rules on transfers work with the open market option regime?

19. Will there be different transfer regimes for contract-based and trust-based schemes?

20. Will the Government be coming up with more effective ways to police against scammers who are likely to try to take advantage of confusions caused by the new flexibilities?

21. Will trustees and managers be given additional responsibilities regarding policing the destination of transfers?

— If so, how does this fit with the right of the member to take a transfer?

— Will trustees and managers be given any additional tools to combat transfers to dubious destination schemes?

**DB to DC Transfers**

22. Will there be a threshold below which advice is not required? (There was a reference to the £30K trivial lump sum threshold in the announcement as somehow relevant.)

23. Current requirements regarding the content of wake-up letters, etc in relation to the OMO are no longer appropriate and in fact may be misleading where members have an option to take a lump sum or transfer to some form of drawdown. What is being done with the OMO regime, which no longer appears to be fit for purpose?

24. What will trustees need to seek from members as proof that advice has been taken?

25. How will the advice requirement interact with trustees’ duties to assure themselves that the arrangement is not fraudulent, now that “liberation” is acceptable under the tax laws?

26. Under what circumstances will the statutory discharge now available to trustees when a statutory CETV is taken be available on transfers by right?

27. What actions by an employer make a transfer employer incentivised (so that the advice must be paid for by the employer)?

28. How, if at all, will the CETV calculation be changed given the new circumstances in which transfers may be requested?

29. Will trustees receive further guidance on how and whether to reduce CETVs in order to protect remaining members of an underfunded scheme?

30. Will advice be required where a benefit within a scheme is transformed from defined contribution to defined benefit?

31. Will there be any restrictions on partial crystallisation of DB benefits in lump sum form, for example, payment of the value of non-statutory inflation increases in lump sum form to the member as an UFPLS, so long as advice is taken?

32. What steps will be taken to prevent schemes styled as occupational DB schemes from evading the DB to DC advice regime?

**DC to DC Transfers**

33. Will there be any move to control charges to members from transferring and receiving schemes?

34. What sorts of measures will be in place to prevent schemes styled as occupational schemes from misrepresenting charges, investment strategies and other aspects of their offering to individuals who may transfer in order to take advantage of enhanced flexibilities offered?
Some answers expected in amendments to Pension Scheme Bill to be laid before Parliament in late October 2014 and some in regulations will follow in the Spring.

NEW PRODUCTS/DEFAULTS

35. Will schemes be allowed to automatically transfer members to another scheme offering a drawdown facility and, if so, how and under what conditions?

36. Will schemes be allowed to ‘promote’ their own or others drawdown solutions without wandering into advice? Will the Government facilitate schemes helping their members choose a drawdown scheme without independent advice?

37. How should schemes deal with members who simply cannot make a choice?

38. Will schemes still be able to default members into an annuity at age 75 if the scheme rules currently require it?

Flexi-access drawdown

39. Will there be new regulations on suitability and disclosure for trust based schemes offering drawdown (and UFPLS) and, if so, what form will these take, what will they include and when will they be published?

40. Will there be any impediments to charging members who use flexible access, as opposed to spreading the admin costs across all members?

41. Will a charge cap or other restrictions be applied to FAD?

42. Will current rules regarding the timing of taking tax free lump sums remain?

43. Now that the “death tax” has been removed from crystallised pension arrangements held for members under age 75, what sorts of differential treatment will remain for funds such crystallised funds, as opposed to uncrystallised funds? Will the only difference be the availability of a tax free sum?

44. Will there be regulation around the conversion of a capped drawdown fund to a flexi-access drawdown fund?

45. Will it be possible to inadvertently convert a capped drawdown fund to a flexi-access drawdown fund?

Uncrystallised funds pension lump sums

46. Will or should there be anything to prevent providers from simply cashing out small pots as uncrystallised pension lump sums where members are given notice of right to transfer instead?

47. Will FCA rules (and equivalent DWP regs) for drawdown also be applied to UFPLS? What disclosures will be required at point of withdrawal and on-going?

Lifetime Annuities

48. Will there be a different regulatory regime around annuities that may reduce over a pensioner’s lifetime? If so, who will develop the regulatory regime, FCA, DWP, Treasury?

Answers expected in form of primary or secondary regulations from DWP and new rules developed by FCA in due course?

GUIDANCE GUARANTEE

49. What brand will the guidance service operate under and how will schemes have to describe the guidance?

50. Will the guidance service be promoted by the government?

51. What form will the guidance take?

52. Who will be required or given responsibility for providing the guidance?

53. How will F2F guidance be delivered and how accessible will this be?

54. Who will be entitled to the guidance and at what point(s) in their lives?

55. What information will be included in the guidance?

56. What outcome is guidance designed to deliver?

57. Will schemes have to track whether members have sought guidance?

58. What signposting will be required of trustees?

59. What signposting will be required of providers of contract-based schemes?

60. How will the performance of guidance be measured?
61. What will the roles of FCA be in monitoring delivery of the guidance guarantee?

62. What steps will be taken to keep a level playing field regarding delivery of the guidance guarantee to members of contract-based and trust-based schemes?

63. Must/should administrators demand proof that guidance has been sought before paying or transferring benefits? If so, how does this fit with the member right to transfer?

64. Can schemes provide or arrange for alternative guidance in lieu of that provided by the Government? If so, will this be regulated in any way?

65. How soon can we expect to see progress towards “pension passports” for members seeking guidance?
   - Will there be a central repository of information? Who will that be?
   - What disclosure requirements will be expected of trustees and managers?

Some answers expected in amendments to Pension Scheme Bill to be laid before Parliament in late October 2014 and some in regulations will follow in the spring.

Freedom and choice odds and ends

Statutory override

66. The current override would allow trustees or managers of a scheme to pay benefits in line with the new tax flexibilities at their discretion on a case by case basis without altering the scheme rules or recourse to the employer. Is it intended that this override (which is very unusual) will remain, or might the process for occupational schemes be managed under section 68 Pensions Act 1995, as is usually the case.

67. Is the statutory override applicable to scheme rules (including rules referencing protected rights) intended to protect spouse’s benefits?

68. Will the override be extended to allow schemes to adopt charging structures related to the new flexibilities?

69. Assuming the power remains as drafted, will TPR be giving any guidance on the circumstances in which trustees would be justified in using or failing to use this power?

Trivial commutation lump sums

70. Currently, the TCLS is only available if all benefits across all schemes, including crystallised benefits, are less than £30K and all must be taken within one year. Now that TCLS will be available only in respect of DB benefits, will funds taken from or remaining in DC schemes continue to count towards the £30K limit?

71. Are any plans afoot (eg the pension passport) to make the pension benefits easier to detect?

Contracted out benefits

72. Will the regulations pertaining to contracted out benefits be amended to allow the new flexibilities apply to guaranteed minimum pensions?

Bankruptcy

73. Under recent case law, pension benefits accessible to the member are now accessible to creditors as well. Will steps be taken to protect at least some of the pension savings of members over the age of 55 from creditors, now that the entire pot can be taken as a lump sum?

Pensions on divorce

74. Many earmarking orders on divorce award the spouse a percentage of “the maximum lump sum available”, based on the assumption that the maximum lump sum will come to 25% of the pension’s value. Now that the maximum lump sum can come to the value of the entire pension, is anything going to be done to prevent these awards from being enforced literally under the new regime?

PPF

75. How will the new flexibilities apply to schemes in PPF assessment?

76. Are steps being taken to ensure that lump sums are not taken by highly-paid employees immediately prior to assessment?

QROPS

77. Will the rule that QROPS must in certain circumstances pay at least 70% of UK tax-relieved monies as income be retained?
Minimum pension age

78. How and when will minimum pension age change?

Further change

79. Will the next government make further changes to pension tax?

80. Will the next government limit the freedom & choice?

81. Is tax relief on pensions sustainable in F&C environment?

Better workplace pensions

Charge cap

82. To whom will the charge cap apply?
   — All members, including deferreds?
   — How would this be accomplished in contract-based schemes?
   — Active members only?
   — Post-April contributions only?

83. How is this consistent with the desire that deferred members be subject to the same charges as actives?

84. What charges will be counted towards the charge cap?

85. How will charges taken from contributions or as annual lump sum charges be limited?

86. Can the industry expect any help from the Government come April in communicating to members why their investments, or the direction of their contributions, has changed?

87. Will there be any regulations or guidance concerning the efforts of trustees and providers to communicate the change?

88. How and how often will it be calculated—and what happens when market volatility changes the fund on which the charge has been taken?

89. Will it be permissible to charge separately for transfers, outside of the charge cap?

90. How and when will schemes need to report compliance with the charge cap?

91. How will compliance be monitored?

92. Will trustees be entitled to take charges from the fund of a member who has been in the default fund to cover the cost of advice at member request?

93. Can a member who is enrolled in the default fund be charged separately for:
   — flexi-access
   — a transfer
   — an uncrystallised funds pension lump sum
   — when he or she chooses any of these options?

94. Are there any plans to provide waivers from the charge cap where there is a guaranteed return?

Minimum quality standards—governance

95. What will trustee chairs have to include in their annual statements?

96. What transaction costs should be reported in annual statements when there is no agreed definition?

97. Will there be any requirement on fund managers to disclose transaction costs, and if so what form will that requirement take?

98. What deadlines will trustee chairs have to meet in publishing their reports?

99. What will the requirements for independence and term limits for members of master trust boards?

100. How should trustees assess value for money?

101. How will providers IGCs interact with employers and their own governance arrangements?

Some answers expected in Government response paper and draft regulations in late October 2014. Legislation not expected to be made until early 2015, making it difficult to schedule system changes.

November 2014
CHARGES FOR RETAIL INVESTMENT ADVICE

We have been asked by HM Treasury to write to the Committee to outline the current situation with regard to charges for financial advice relating to retail investment products. In particular, the Committee is interested in the transparency, and the level of charges for investment advice.

The Committee will be aware that the rules around advisers’ remuneration (as well as their qualifications and how they described their services) changed at the end of 2012, following the Retail Distribution Review (RDR). The RDR was a once-in-a-generation change to the way investment intermediaries charge for their services and followed a long period of research and consultation. It may be helpful to note that these changes related to advice on all retail investment products, not just products relating to retirement income.

With respect to advice charges and their transparency, one of the objectives of the RDR was to make clear to consumers that advice had a cost, and what that cost was. Prior to this change, advisers had typically been remunerated by commission from product providers. This was both opaque and had the potential to bias the recommendations made to the consumer. Our research showed that, despite commission disclosure requirements, most consumers thought advice was free when in fact commission implied a cost, and often a substantial cost, which would have an impact on the performance of their investment.

Thus, prior to the introduction of the RDR, it is fair to say that the cost of advice was far from transparent to the consumer and varied depending not on the level and quality of service but on the amount of commission the product provider offered for selling that particular product. The RDR sought to improve price transparency and help consumers make decisions for themselves about the cost of advice in relation to its quality and its value to the consumer.

The RDR rules have banned commission from product providers in relation to advice on retail investment products. Instead, advisers have to tell customers very explicitly what their charges are for the service they are providing. They have to explain to the consumer both the cost and how it will be paid for both initial advice and any on-going service, should the consumer choose to take this. We do not mandate what form those charges could take—for example, they could be a charge per hour, a percentage of funds under advisement or some combination,—nor do we mandate what level these prices should be or set a maximum. But our rules do require that the cost of advice should be clear, transparent and comprehensible to the consumer.

The rules came into effect at the end of 2012 and we gave a commitment to carry out a post implementation review (PIR), examining the outcomes from the rule changes against our expectations using the baseline set of measures we published in 2011. We will publish the PIR in December.

We have also undertaken thematic work to understand how well firms are complying with our rules in this area and published the first results earlier this year. The results were disappointing and it was clear that more work had to be done in firms to ensure they complied with our rules and provided consumers with clear information on charges. We have subsequently carried out a further round of thematic work, to assess how much things have improved in this area, and carried out research to assess consumer understanding and experience in relation to adviser charging and other rule changes. This information is currently being finalised and will not be available until later next month, when we publish the results of the first stage PIR.

For this reason, it is difficult to provide a precise answer at this stage to the Committee’s question about the clarity and level of charges for advice. However, it would be misleading to think that there is one simple price for advice: our understanding is that firms will often offer different levels of services for different prices, depending on the needs of the consumer. We will write to the Committee again once we have published the PIR, if that would be helpful. We are aware that the Money Advice Service has plans to publish a directory of advice costs on advisers that give retirement advice and volunteer to be involved. We will have a link to this on our website.

We would also like to note that the market for advice is one which is dynamic and therefore is always changing, for instance in relation to the models of advice, what it comprises, and how it is delivered. Earlier this year we published a Guidance Consultation on the boundaries of advice and on how firms could provide automated advice, say through a website. Where consumer needs are more straightforward a simplified process which is delivered electronically, without face-to-face engagement, could be a very cost-effective solution. We therefore expect to see a range of advice models developed within those guidelines to meet the “at retirement” needs, which could be either simplified or focussed advice at a lower cost than the full advice service.

There will be a range of services to support consumer decision making at retirement. The pensions guidance service should be viewed as part of this spectrum which ranges from the information provided by the pension...
provider to full regulated financial advice and should help consumers interact with other services, such as regulated financial advisers. For many the appropriate route will still be to take regulated financial advice.

November 2014

Written evidence submitted by Britannia Financial Services Ltd, Auckland, New Zealand (TP 17)

INTRODUCTION

1. This submission is made on behalf of Britannia Financial Services Ltd. We are a medium sized financial services company based in Auckland, New Zealand. We have offered financial advice to UK expatriate community for the last 20 years having expertise in the areas of retirement planning and wealth creation with particular emphasis on the transfer of pension accounts from United Kingdom registered pension schemes. Transferred funds are invested on an ethical basis and combined with a planned retirement savings programme leading to enhanced security in retirement.

SUBMISSION

2. Our submission wishes to bring to your attention concerns regarding the blanket prohibition alluded to in the Taxation of Pension Bill regarding access for transfer purposes for certain unfunded state sector defined benefit registered pension schemes—and the impact this blanket ban will have on the future financial well-being of returning New Zealanders and UK expatriates emigrating to this country who have previously contributed to these schemes.

3. We have read through the explanatory notes in relation to the Bill and are alerted to the fact that a blanket ban on transfers from unfunded state sector schemes seems to be an inevitable consequence.

4. The initial HM Treasury consultation document entitled Freedom and choice in pensions” raised the possibility that the government might legislate to remove the right to transfer from defined benefit schemes to defined contribution schemes “except in exceptional circumstances”.

5. The follow up document from HM Treasury entitled “Freedom and choice in pensions—government response to the consultation” completely omitted any reference to “exceptional circumstances” concept in allowing some transfers to be made from defined benefit schemes.

6. During the initial consultation period on the initial paper entitled “Freedom and choice in pensions” we made the point strongly that denying the right to a cash equivalent transfer value from an unfunded state sector defined benefit scheme for former contributors, either returning to New Zealand after spending some years working in the United Kingdom, or to persons emigrating with their families to this country, would create a two tier pension situation for these persons. Some returning New Zealanders or emigrants having the right to transfer pension rights from fully funded defined benefit and/or defined contribution schemes as opposed those unfortunate enough to have contributed to unfunded state sector defined benefit schemes.

7. We made the further point that New Zealand operates a tax incentive scheme whereby pension holders returning home—or persons immigrating to this country holding offshore pension accounts have a four year window of opportunity to transfer their pension funds to a qualifying New Zealand scheme or suffer quite severe tax penalties. If transfers from certain defined benefit schemes are prohibited these contributors will be severely disadvantaged in later life when their pensions can be drawn down from the UK scheme.

8. Our submission made reference to an analysis conducted by industry sources indicated a very small percentage of contributors exiting unfunded defined benefit schemes to either return home or emigrate compared to total contributions to these schemes (less than 0.3%). This figure hardly likely to be a drain on the Exchequer.

9. Our submission suggested that the undefined “exceptional circumstances” concept present in the original consultation document should be defined in regulations and include the provision for an ex member of a defined benefit scheme to be granted an exemption from any transfer ban on the basis that they had moved permanently abroad with no intention of returning the UK to live and/or retire. We suggested further that any application under this exemption if granted must be accompanied by firm evidence of a permanent move abroad.

10. An exemption from any ban on the grounds of permanent emigration would simply take pension transfer rules back to the situation that existed before “A Day” established the QROPS regime. Previous regulations required the applicant to show firm evidence of permanent residency and employment abroad.

SUMMARY

11. We have concerns that a blanket ban on transfers from certain defined benefit schemes may be legislated for in the final version of the Taxation of Pension Bill.

12. The original consultation paper issued by HM Treasury floated the idea that some transfers would be allowed from defined benefit schemes in “exceptional circumstances”.
13. The follow up document issued by HM Treasury made no further mention of the “exceptional circumstances” concept.

14. A blanket ban on the transfer of defined benefit schemes will mean the creation of a two tiered pension situation with some emigrants and/or returning New Zealanders having rights to transfer their pension and some not.

15. New Zealand operates a system of tax penalties for persons holding overseas domiciled pension accounts which will penalise more heavily those members of defined benefit schemes unable to transfer their pension to New Zealand through no fault of their own.

16. A secure system could easily be established to ensure persons applying for a transfer under permanent emigration rules were genuine.

17. An exemption from any ban on transfers from defined benefit schemes provided sufficient evidence was provided showing permanent residence abroad would be a reversion back to regulations applying before “A Day” and the creation of the QROPS entity.

Person responsible for this submission:
D. T. Milner, CFP, CLU, GradDipBusStud (Massey), AFA
Director, Britannia Financial Services Ltd, Auckland, New Zealand
November 2014

Written evidence from Partnership Assurance Group plc (Partnership) (TP 18)

ABOUT PARTNERSHIP

1.1 Partnership is a long established UK insurer specialising in the design and manufacture of financial products for people whose health and lifestyle means that their life expectancy is likely to be reduced. Partnership aims to offer higher retirement incomes than traditional providers through undertaking a detailed assessment of people’s health and lifestyle conditions. It is a leading provider of enhanced annuities; typically, our average customer can receive approximately 18% extra income for life, compared to a standard annuity provider, and for those with more serious conditions, potentially much more. We estimate that over 50% of people at retirement could qualify for one of our annuities.

EXECUTIVE SUMMARY

2.1 Partnership welcomes the opportunity to respond to the House of Commons Public Bill Committee’s call for written evidence on the Taxation of Pension Bill (‘The Bill’).

2.2 Partnership welcomes the Bill as we believe that more choice for those entering retirement is a good thing and increased choice should help to enable people to save for, and make informed decisions in relation to, their retirement income.

2.3 However, we believe that more consideration needs to be given to ensure that certain products are not disadvantaged by the new rules. In particular, we are concerned by measures being brought in which will see taxable ‘death benefits’ on annuities, but not on other products such as drawdown. We would also like to see additional measures to allow people to use savings mechanisms, such as ISAs, to purchase retirement income through an annuity. For those who may require long term care in later life, we would like to see proposals brought in to allow people to use their private pension savings to purchase care products, such as care annuities. We believe that these measures would enhance the current freedom and choice in pensions’ agenda.

2.4 Although the guidance guarantee is not part of this Bill, we also believe that consideration needs to be given to the risk that a potentially large number of consumers lack sufficient financial literacy and understanding to manage their funds very well over retirement. Therefore, the need for meaningful support and guidance for consumers when making complex retirement decisions is imperative.

FINANCIAL PRODUCTS

3.1 Partnership believes that annuity products will remain the most appropriate product for many people. Underpinning the concept of pensions saving is the wish to provide income security for the whole of retirement and to ensure that someone does not run out of retirement funds before they die. Annuity providers take on the investment, credit, inflation and longevity risk for the consumer and provide an income that will last for life regardless of changes in circumstances or investment markets. Research conducted by Partnership found that 64% of people listed a guaranteed income for life as the top characteristic of a “perfect retirement product.”

3.2 Research conducted among Partnership’s customers in 2012, to ascertain what they spent the additional income received from an enhanced annuity on, demonstrated that a significant proportion spent the extra money on higher food bills (61%), heating and electricity (57%), and on meeting the costs of higher council tax and other bills (53%). We believe that this research highlights the importance of the guidance guarantee in helping
consumers recognise the importance of securing a base level of income in retirement; notwithstanding their eligibility for the flat rate state pension.

**TAXABLE DEATH BENEFITS ON ANNUITIES**

4.1 HM Treasury has announced that people with annuities will be allowed to pass on a lump sum as a ‘death benefit’ tax free. However, if the benefit is passed on as an income (as with a joint life annuity or associated guaranteed period income payment) then it will be taxed at the beneficiary’s usual income tax rate.

4.2 We strongly believe that annuities should be given the same preferential treatment as drawdown. Annuities provide a steady, guaranteed income in retirement and we believe that individuals who purchase them should not be penalised for making this choice.

**OFFERING ENHANCED ANNUITIES FOR ISAs**

5.1 Partnership believes that to further enhance the choice delivered by the pension reforms, consideration should be given to enable consumers to purchase annuities and guaranteed income with ISA funds.

5.2 We understand that in order to give effect to this it may only require S 9 d (i) of the ISA regulations relating to ‘insurance policies’ to be removed from the Individual Savings Account Regulations 1998. We do not believe any further changes to the Regulations would be necessary and imagine that this would only require a change to SIs.

5.3 Doubts have been raised by some policy makers who believe that enhanced annuities for ISAs cannot be achieved because ISA assets have to be ‘surrenderable’ within 30 days. However, Partnership does not see this as an insurmountable barrier, providing annuity providers are able to offer a market based surrender value which takes into account the market value of the assets which back the annuity and any changes in the state of health of the annuitant.

**CARE ANNUITIES**

6.1 Funding long term care is a growing concern with many consumes still unaware that they may have to fund all or some of their social care needs. The proposals set out in the Care Act 2014 will go a long way to helping to address some of the concerns. However, the new retirement system provides a good opportunity to encourage people to consider how they may fund any long term care needs that might arise.

6.2 To help people to fund their care needs in later life, we believe that people should be allowed to use their pension funds to buy Care Annuities which could help to ensure that they do not deplete their savings prematurely, falling back on state funding. We would encourage policy makers to look at this proposal as part of the reform package.

*November 2014*