House of Commons Library

Research Briefing

22 March 2023

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Reform of pension tax relief

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How are pensions taxed in the UK?

In the UK, private pension saving is taxed on an “exempt, exempt, taxed” (EET) model. This means:

- When people and their employers pay into a pension, the contributions are **exempt** from taxation. Both the saver and any contributing employer receive tax relief, up to set limits.
- If the pension savings grow through investments, this is **exempt** from taxation.
- When the savings are withdrawn as pension payments, these are **taxed** like other income. People are allowed access up to 25% of their pension savings tax free.

What are the limits on pensions tax relief?

There are limits on the amount of tax relief someone can receive when they are contributing to their pension. In 2022/23 these were:

- A person can receive tax relief on pension contributions of up to 100% of their annual earnings. Someone earning less than £3,600 a year can receive relief on contributions up to £3,600.
- An annual allowance, which limits the amount someone can pay into a pension pot to £40,000 each year before they pay tax. This allowance is tapered (reduced) for people earning more than £240,000 including pension contributions. The minimum annual allowance someone with tapering can retain is £4,000.
- A lifetime allowance of £1,073,100, which is the total amount someone can usually build up in pension pots without paying tax.
- Once someone withdraws savings from a defined contribution pension, the amount that they can contribute to defined contribution schemes and receive tax relief on in future is reduced to the money purchase annual allowance of £4,000 a year.

The way pension tax rules are applied can depend on the type of pension scheme. More detailed information about these allowances is available in the

Commons Library briefing Pension tax relief: The annual allowance and lifetime allowance.

What was announced in the 2023 Budget?

The Chancellor announced changes to pension allowances, so that from 6 April 2023:

- The lifetime allowance would be abolished
- The annual allowance would increase from £40,000 to £60,000
- The adjusted income when the tapering of the annual allowance for high earners begins would increase from £240,000 to £260,000 and the minimum annual allowance someone with tapering can retain would increase from £4,000 to £10,000
- The money purchase annual allowance will increase from £4,000 to £10,000

The maximum amount someone can withdraw from a pension tax free will remain at £268,275 – 25% of the lifetime allowance in 2022/23. Above this, income from pensions will be c liable to income tax, charged at the individual's marginal rate, but will not be subject to additional taxes.

In his Budget Speech, the Chancellor cited concerns about the impact of pension taxation on senior NHS clinicians. These are covered in the Commons Library briefing Public service pensions: Impact of pension tax rules on NHS consultants and GPs

What are the options for further reform?

A single rate of pensions tax relief

One option for reform is a single rate of tax relief, rather than relief being given at someone's marginal rate of tax. Those in favour of a single rate of pensions tax relief often argue that it would be fairer for all taxpayers to receive the same rate of relief. Under the current system higher rate income taxpayers receive a higher rate of pensions tax relief. Those opposed to a single rate of tax relief argue that it would be expensive to administer, unfair and inappropriately distort behaviour.

Taxing pension contributions

In the UK, private pension saving is taxed on an "exempt, exempt, taxed" model (EET). This means that tax is not paid on contributions and investment growth, but tax is paid when savings are used to make pension payments. A different approach which has been considered is a “taxed, exempt, exempt” model (TEE). In this system contributions are taxed like other salary and no tax is paid on investment growth and payments from savings.

Those in favour have said that the current system is expensive. Opponents however have argued that the transition to a new system would be complex and taxing contributions would disincentivise pension saving.

National insurance Contributions

The Institute for Fiscal Studies, a UK economics research institute, has proposed changing how employee and employer National Insurance Contributions interact with pensions tax relief. It has suggested that employee NICs should align with the pension tax relief approach for income tax and that employers receive tax relief in the form of a subsidy for their pension contributions instead.

1 Background

1.1 How are pensions taxed in the UK?

In the UK, private pension saving is taxed on an "exempt, exempt, taxed" (EET) model. This means:

- When people and their employers pay into a pension, the contributions are **exempt** from taxation. Both the saver and any contributing employer receive tax relief, up to set limits.
- If the pension savings grow through investments, this is **exempt** from taxation.
- When the savings are withdrawn as pension payments, these are **taxed** like other income. People are allowed access up to 25% of their pension savings tax free.[1]

1.2 What are the limits of pensions tax relief?

There are limits on the amount of tax relief someone can receive when they are contributing to their pension. In 2022/23 these were:

- A person can receive tax relief on pension contributions of up to 100% of their annual earnings. [2] Someone earning less than £3,600 a year can receive relief on contributions up to this amount.[3]
- An annual allowance, which limits the amount someone can pay into a pension pot to £40,000 each year before they pay tax. This allowance is tapered (reduced) for people earning more than £240,000 including pension contributions. The minimum annual allowance someone with tapering can retain is £4,000.
- A lifetime allowance of £1,073,100, which is the total amount someone can usually build up in pension pots without paying a tax charge.

1 Pensions Tax Manual, PTM024100 – General principles: overview of pensions taxation: the basics, HMRC, 13 December 2022
2 Finance Act 2004, section 190
3 As above

- Once someone withdraws savings from a defined contribution pension, the amount that they can contribute to defined contribution schemes and receive tax relief on in future is reduced to the money purchase annual allowance of £4,000.

The way pension tax rules are applied can depend on the type of pension scheme. There are two main types of pension schemes in the UK:

- **Defined benefit schemes** pay a promised pension based on factors such as salary and length of service. A sponsor, which is usually an employer, guarantees the promised benefits are paid. The pension provides an income for life and may also include a retirement lump sum.

- **Defined contribution schemes** do not provide a guaranteed pension and instead provide a pot of money which can be used in retirement. The value of the pension pot depends on the amount paid into the scheme and the returns on investment of that amount.

Further information on current UK pension tax relief is available in the Commons Library briefing Pension tax relief: The annual allowance and lifetime allowance.

1.3 What was announced in the Budget 2023?

The Chancellor announced changes to pension allowances, so that from 6 April 2023:

- There would be no tax charge for exceeding the lifetime allowance and it would be abolished in a future Finance Bill

- The annual allowance would increase from £40,000 to £60,000

- The adjusted income when the tapering of the annual allowance for high earners begins will increase from £240,000 to £260,000 and that the minimum annual allowance someone with tapering can retain will increase from £4,000 to £10,000

- Once someone withdraws savings from a defined contribution pension, the amount that they can contribute to defined contribution schemes in future is reduced to the money purchase annual allowance. The money purchase annual allowance will increase from £4,000 to £10,000[4]

The maximum amount someone can withdraw from a pension tax free will remain at £268,275 – 25% of the lifetime allowance in 2022/23.[5]

4 Finance Act 2004, section 190

5 As above

In his Budget Speech, the Chancellor cited concerns about the impact of pension taxation on senior NHS staff.[6] These are covered in the Commons Library briefing Public service pensions: Impact of pension tax rules on NHS consultants and GPs.

1.4 How much does pension tax relief cost?

In 2020/21, an estimated £67.3 billion of tax relief was provided on pensions. In the same year, £18.3 billion was collected on private pensions as they were paid out to scheme members. The net cost of pension income tax and National Insurance Contributions (NICs) relief was estimated to be £48.2 billion.[7]

The figure for net cost of tax relief may misrepresent the actual cost to the Government. The Treasury explained in 2015 that the measure may not be appropriate because of the gap in time between tax relief on contributions and tax collected on pensions when they are paid.[8]

The majority of income tax relief on pension contributions in 2020/21 is estimated to have been relieved at higher income tax rates. 52% of total tax relief was provided at incomes in the 40% income tax bracket, and 6% was provided at the 45% additional income tax bracket.[9]

Estimated cost of pension income tax and NICs relief

£ million (rounded to the nearest £100 million)

	2019/20	2020/21[P]
Pension income tax and NICs relief (gross of tax charges)	**63,100**	**67,300**
Pension income tax relief	41,700	44,100
Pension NICs relief	21,400	23,200
Pension tax charges	**18,600**	**19,100**
Income tax liable on payments from pension schemes	17,900	18,300
Annual allowance charges	400	300
Lifetime allowance charges	300	400
Net pension income tax and NICs relief	**44,500**	**48,200**

p: provisional

Source: HM Revenue & Customs, Private pension statistics, 30 November 2022, Table 6

6 HM Treasury, Spring Budget 2023 speech, 15 March 2023

7 HM Revenue & Customs, Private pension statistics, 30 November 2022, Table 6

8 HM Treasury, Strengthening the incentive to save: a consultation on pensions tax relief, Cm 9102, July 2015, para 2.4

9 HM Revenue & Customs, Private pension statistics commentary: September 2022, 30 November 2022; For income tax rates see Gov.uk, Income Tax rates and Personal Allowances [accessed 15 March 2023]

1.5 Why do pensions receive tax relief?

Broadly, tax relief on pensions is intended to encourage private saving for later life.

In the 2014 Budget the Coalition Government announced a major reform in the tax rules for some pensions known as the pension freedoms.[10] Introducing the reforms, the Government explained that "tax relief is given so that the funds are used to provide benefits later in life for the member [of the pension scheme] and their dependants."[11] The Coalition Government had previously set out its tax principles for retirement as:

1. The purpose of tax-relieved pension saving is to provide an income in retirement.
2. Any changes to the pensions tax rules should not incur Exchequer cost and should not create any opportunities for tax avoidance.
3. Individuals should have the flexibility to decide when and how best to turn their pension savings into a retirement income, provided that they have sufficient income to avoid exhausting savings prematurely and fall back on the state.
4. In line with the EET model, pension benefits taken during an individual's lifetime should be taxed at income tax rates. The tax-free pension commencement lump sum will continue to be available.
5. On death, pension savings that have been accumulated with tax relief should be taxed at an appropriate rate to recover past relief given, unless they are used to provide a pension for a dependant.[12]

In July 2015, the Conservative Government proposed reforming its principles to strengthen incentives to save and ensure sustainability:

- It should be **simple and transparent.** The government believes that greater simplicity and transparency may encourage greater engagement with pension saving and strengthen the incentive for individuals to save into a pension.
- It should allow individuals to take **personal responsibility** for ensuring they have adequate savings for retirement. It should encourage people to save enough during their working lives to meet their aspirations for a sufficient standard of living in retirement.

10 For more detail, see Commons Library briefing CBP-6891, Pension flexibilities: the freedom and choice reforms, 23 December 2019

11 Explanatory Notes to the Taxation of Pensions Act 2014, para 8

12 HM Treasury, Removing the requirement to annuitise by age 75, July 2010, para 2.10

- It should **build on the early success of automatic enrolment** in encouraging new people to save more.[13]

- It should be **sustainable**. Any proposal for reform should also be in line with the government's long-term fiscal strategy.[14]

In July 2020, the Treasury launched a consultation on the administration of pensions tax relief which focussed on the relief for low earners (covered in section 2.4). In its call for evidence it set out three principles for making changes: simplicity, deliverability and proportionality.[15]

Comment

A range of organisations have commented on the objectives of pension tax relief. The Pensions Policy Institute said in 2016 that the "two main reasons why tax relief is given on pensions are to encourage people to save for their retirement, and to make the tax system for pension saving neutral by ensuring that people do not pay tax twice on the same income."[16]

In 2014, The Institute for Fiscal Studies said that some incentive needs to be provided to encourage people to save for retirement. [17] It said that the pensions tax relief system – while not flawless - achieves two objectives. It ensures that there is no tax on normal returns to saving, but where there are higher returns more tax will be paid on pension income. [18] The system also means that people "who are subject to a higher rate of income tax during part of their working life but subject to the basic rate of income tax during their retirement are able to smooth their income so that they need not end up paying more tax over their lifetime than an otherwise-equivalent individual who receives the same lifetime income in a less variable way."[19]

The Institute for Fiscal Studies has subsequently said that incentives should be well targeted, depending on the government's aim:

> Any such incentives should be well targeted, the meaning of which depends on whether the government's aim is to incentivise all pension saving equally or, for example, to give incentives only, or especially, for certain groups – most obviously those who would otherwise be most at risk of under-saving for retirement – or up to certain limits. Whether any incentives are effective will also depend on how well people understand the incentives and on whether they respond by saving more and using those savings appropriately in

13 Further information on automatic enrolment is available in the Commons Library briefing SN 06417 Pensions: Automatic enrolment - current issues

14 HM Treasury, Strengthening the incentive to save: a consultation on pensions tax relief, Cm 9102, July 2015, para 3.4

15 HM Treasury, Pensions tax relief administration: Call for Evidence, July 2020, para 1.19

16 Pensions Policy Institute, Future trends in pensions tax relief, July 2016

17 Institute for Fiscal Studies, Green Budget 2014, chapter 10

18 As above

19 As above

> retirement. Many arguments for pensions tax reform reflect concerns that the current tax incentives are not well designed.[20]

In July 2021, the Pensions and Lifetime Savings Association published a discussion paper outlining five principles for pension taxation. It suggested:

> Promotes adequacy: provides financial support and incentivises saving for retirement.
>
> Encourages the right behaviours: helps savers make the right decisions about retirement saving.
>
> Fair: helps everyone – the employed and the self-employed- save for retirement.
>
> Simple to adopt & administer: avoids unreasonable transition and on-going costs for employers and schemes.
>
> Enduring & sustainable: designed to avoid repeated change and so builds confidence in long-term saving.[21]

20 Institute for Fiscal Studies, What are the options for reforming pensions taxation? [accessed 21 March 2023]

21 Pensions and Lifetime Savings Association, Five Principles for Pension Taxation: Discussion Paper – Second Edition, July 2021

2 Recent reforms

2.1 Abolition of the lifetime allowance

Budget 2023 abolition of the lifetime allowance

The Chancellor announced in the 2023 Budget that from 6 April 2023 there would be no tax charge for exceeding the lifetime allowance and it would be abolished in a future Finance Bill.[22] In his Budget Speech, the Chancellor cited concerns about the impact of pension taxation on senior NHS staff as a reason for the change.[23]

Reaction

Writing in the Times the Shadow Chancellor, Rachel Reeves, said that Labour had plans to reverse the pension tax changes.[24] Addressing concerns about the impact of pension tax relief on NHS pensions, she said that "a bespoke scheme for doctors could be set up for a fraction of the price."[25]

The British Medical Association welcomed the changes which it said would "end to the NHS 'pension trap' for the majority of doctors".[26]

Nigel Peaple, Director of Policy and Advocacy at the Pensions and Lifetime Savings Association, said that the changes would "encourage older, often highly skilled or experienced workers, including senior doctors, to stay in the workforce and provide more flexibility for retirees to re-enter the world of work."[27]

Paul Johnson, Director of the Institute for Fiscal Studies, a UK economics research institute, said there was a case for the changes and it was sensible to accompany it with a limit on the size of tax-free lump sums (section 2.2 of this paper below). However, he said it was "disappointing that other over-generous aspects of pension taxation – not least complete freedom from inheritance tax – were not reined in."[28] There is no tax paid on most lump sum

22 HM Revenue and Customs, Policy Paper: Pension Tax Limits, 15 March 2023
23 HM Treasury, Spring Budget 2023 speech, 15 March 2023
24 "Rachel Reeves: Why we'll oppose Jeremy Hunt's pension tax giveaway", The Times [online], 20 March 2023
25 As above
26 BMA, Government raises annual allowance for pensions, 15 March 2023
27 Pensions and Lifetime Savings Association, Budget measures will help support savers achieve adequate retirement income, 15 March 2023
28 Institute for Fiscal Studies, Spring Budget 2023 | Institute for Fiscal Studies, 15 March 2023

payments from pensions if the owner of the pension dies before the age of 75.[29]

Previous debate about the need for two separate allowances

Prior to the announcement of the abolition of the lifetime allowance, there had been questions about whether both an annual and lifetime allowance were needed when they both had the same aim – to limit the amount of tax relief someone can receive.

In July 2018, the Treasury Committee recommended that:

> There is widespread acknowledgement that tax relief is not an effective or well targeted way of incentivising saving into pensions. Ultimately, the Government may want to return to the question of whether there should be fundamental reform. However, the existing state of affairs could be improved through further, incremental changes. In particular, the Government should give serious consideration to replacing the lifetime allowance with a lower annual allowance, introducing a flat rate of relief, and promoting understanding of tax relief as a bonus or additional contribution."[30]

In its October 2018 response to the Treasury Committee's report, the Government said that "no consensus for either incremental or more radical reform of pension tax relief has emerged since the consultation in 2015."[31] The Committee further called for reform to the entire approach to pension tax relief in its February 2021 report on tax after coronavirus:

> Given the regressive nature of the benefits accruing to individuals from the current arrangements on pension tax relief, especially those in the top earnings decile, the Chancellor should urgently reform the entire approach to pension tax relief.[32]

On the prospect of future tax reform, the Government said in June 2021 that the 2015 consultation on pensions tax indicated no clear consensus for reform."[33]

In October 2019, the Office of Tax Simplification said that lifetime and annual allowance charges could present significant complexities for pension savers in different circumstances. It questioned whether both should apply:

29 Gov.uk, Tax on a private pension you inherit [accessed 22 March 2023]

30 Treasury Committee, Household finances: income, saving and debt, 18 July 2018, HC 565 2017-19, para 117

31 Treasury Committee, Household finances: income, saving and debt: Government Response to the Committee's Nineteenth Report, 9 October 2018, HC 1627 2017-19

32 Treasury Committee, Tax after coronavirus, 24 February 2021, HC 664 2019-21, para 123

33 Treasury Committee, Tax after coronavirus: The Government's response, HC 144 2021-22, page 11

> Given the policy aim of limiting the overall amount of pensions savings tax relief available to any one individual, applying both the [annual allowance] and [lifetime allowance] charges to pensions may be unnecessary. [34]

It suggested that a possibility would be for the annual allowance to apply only to defined contribution schemes, where contributions into the scheme would be counted, and for the lifetime allowance to apply only to defined benefit schemes. [35] In 2022/23, income from defined benefit pension schemes is valued against the lifetime allowance by applying a flat factor of 20:1. For example, if a defined benefit scheme provides an annual pension of £1,000, it is counted as £20,000 towards the lifetime allowance.[36]

2.2 Limit of tax-free lump sums

People are allowed to receive up to 25% of their pension savings as a tax-free lump sum when they access their pension. Whether this is possible in a particular case will depend on the rules of the specific pension scheme.

While the Chancellor announced in the 2023 Budget that the lifetime allowance would be abolished, the maximum amount someone can withdraw from a pension tax free will remain at £268,275 – 25% of the lifetime allowance in 2022/23.[37] Where excesses to the lifetime allowance were subject to a 55% tax charge, these will change to taxation at an individual's marginal rate.[38]

Earlier proposals to limit tax-free lump sums

In 2013, the Pensions Policy Institute found that changes to the 25% tax-free lump sum would mean pension tax relief was more evenly distributed. However, it did not think it would improve incentives to save.[39]

In its 2014 Green Budget, the Institute for Fiscal Studies had also argued for a limit but said that there is no reliable estimate of how much tax revenue this would raise.[40] More recently, the Institute for Fiscal Studies said an option for reforming the tax-free lump sum could be replacing it with a bonus top-up. It explained:

> At the moment, for every £1 taken from a pension, 25p is tax-free if taken as a lump sum, saving a basic-rate taxpayer 5p (20% of 25p) and a higher-rate taxpayer 10p (40% of 25p) in income tax. Instead, the government could top

34 Office of Tax Simplification, Taxation and Life Events, October 2019
35 As above
36 HM Treasury, Simplifying the taxation of pensions: the Government's proposals, December 2003, para 1.17; Finance Act 2004, s216, Sch 32 and s276
37 HM Revenue and Customs, Policy Paper: Pension Tax Limits, 15 March 2023
38 As above
39 Pensions Policy Institute, Tax Relief for Pension Saving in the UK, July 2013; For more on the background to this, see Pension lump sums, Commons Library Briefing SN02181
40 Green Budget 2014, Institute for Fiscal Studies, Chapter 10,

> up pension savings by, say, 5%, and then charge income tax on the full amount taken from the pension. For a basic-rate taxpayer, a 5p top-up for every £1 of pension savings would be broadly equivalent in value to the tax-free lump sum. [41]

In July 2021, the Pensions and Lifetime Savings Association looked at capping the tax-free lump sum at £75,000. It said around 25% of people aged 55-64 would be affected and may disincentivise pension saving. It also said that "This would be a major retrospective change and so could be considered unfair for those who saved in the belief they would get 25% [tax-free lump sum] without it being capped".[42]

2.3 Changes to the annual allowance and lifetime allowance

Summary of changes

The pension tax simplification regime was a major reform to the pension tax relief system from 6 April 2006 – known as "A-day".[43] This replaced eight different tax regimes governing pensions with a single set of rules applying across pension schemes and included the introduction of the annual and lifetime allowances.

The table below shows the levels of the main pension tax relief allowances and the levels of income for tapering of the annual allowance (section 1.2 of this paper) since introduction:

41 Institute for Fiscal Studies, What are the options for reforming pensions taxation? [accessed 21 March 2023]

42 The Pensions and Lifetime Savings Association, Five principles for pension taxation, February 2021

43 Finance Act 2004

Pension tax relief allowances
£

	Standard Lifetime allowance	Standard Annual allowance	Tapered annual allowance minimum	AA tapering threshold income	AA tapering adjusted income	Money purchase annual allowance
2006/07	1,500,000	215,000	-	-	-	-
2007/08	1,600,000	225,000	-	-	-	-
2008/09	1,650,000	235,000	-	-	-	-
2009/10	1,750,000	245,000	-	-	-	-
2010/11	1,800,000	255,000	-	-	-	-
2011/12	1,800,000	50,000	-	-	-	-
2012/13	1,500,000	50,000	-	-	-	-
2013/14	1,500,000	50,000	-	-	-	
2014/15	1,250,000	40,000	-	-	-	10,000
2015/16	1,250,000	40,000	-	-	-	10,000
2016/17	1,000,000	40,000	10,000	110,000	150,000	10,000
2017/18	1,000,000	40,000	10,000	110,000	150,000	4,000
2018/19	1,030,000	40,000	10,000	110,000	150,000	4,000
2019/20	1,055,000	40,000	10,000	110,000	150,000	4,000
2020/21	1,073,100	40,000	4,000	200,000	240,000	4,000
2021/22	1,073,100	40,000	4,000	200,000	240,000	4,000
2022/23	1,073,100	40,000	4,000	200,000	240,000	4,000
2023/24	-	60,000	10,000	200,000	260,000	10,000

Sources: Finance Acts 2006 onwards. Further detail in following sections of this paper.

Tapered annual allowance

Since 2016/17, the annual allowance has been tapered. This means the annual allowance reduces for earners with an income above both a taxed threshold and an adjusted amount including pension contributions.[44] For every £2 of income someone receives above their adjusted income their annual allowance is reduced by £1.[45]

Between 6 April 2016 and 5 April 2020, the threshold income for tapering the annual allowance was £110,000, adjusted income was £150,000 and people could retain an annual allowance of at least £10,000.[46]

Although these rules applied across all schemes, the nature of many doctors' work meant there was a particular impact on the NHS (for example, consultants taking on additional work often at short notice to cover service pressures). This was particularly felt in 2019/20 when the capacity to bring

44 Finance Act 2015, schedule 4
45 Finance Act 2020, part 1 section 22
46 Finance Act 2015, schedule 4

forward unused annual allowances from the previous three years was largely exhausted.[47]

In October 2019, the Office of Tax Simplification said:

> The government should continue to review the annual allowance and lifetime allowances and how, in combination, they deliver against their policy objectives, taking account of the distortions (such as those affecting the National Health Service) they sometimes produce.[48]

In the March 2020 Budget, the Government announced increases of £90,000 in the income thresholds for the tapered annual allowance ('adjusted income' increased to £240,000, 'threshold income' to £200,000) and a decrease in the minimum annual allowance to £4,000.[49]

The Chancellor announced changes to pension allowances in the 2023 Budget, so that from 6 April 2023 the adjusted income when the tapering of the annual allowance for high earners begins will increase from £240,000 to £260,000 and that the minimum annual allowance someone with tapering can retain will increase from £4,000 to £10,000.[50]

Money Purchase annual allowance

In the 2014 Budget, the Coalition Government announced a major reform in the tax rules for some pensions, known as the pension freedoms.[51] The pension freedoms meant that, from 6 April 2015, people aged 55 and over would be able to make withdrawals from their defined contribution pension pot "at a time of their choosing, subject to their marginal rate of income tax".[52]

The money purchase allowance is intended to prevent people using the pension freedoms to avoid tax on their employment income by paying it into a pension before immediately withdrawing it with 25% of it not taxed.[53] Once someone accesses a defined contribution pension, the amount that they can contribute each year to defined contribution schemes in future without paying

47 Department of Health and Social Care, NHS Pension Scheme: proposed flexibility, 22 July 2019, para 1.11

48 Office of Tax Simplification, Taxation and Life Events: Simplifying tax for individuals, October 2019, recommendation 8

49 HM Treasury, Budget 2020, 11 March 2020

50 As above

51 HM Treasury, Budget 2014, 19 March 2014

52 As above

53 HM Treasury, Freedom and choice in pensions: Government response to consultation, Cm 8901, July 2014, para 2.27

tax is reduced to the money purchase annual allowance.[54] Originally, it was set at £10,000.[55] It was reduced to £4,000 in April 2017.[56]

The Chancellor announced in the 2023 Budget that from 6 April 2023 the money purchase annual allowance will increase to £10,000.[57]

Comment

Since the money purchase annual allowance was introduced in April 2015 there have been calls for it to be reformed. In October 2019, the Office of Tax Simplification said:

> The reduction in the level of the money-purchase annual allowance in 2017 has increased concern that those withdrawing small amounts, perhaps from a small pension savings scheme they have, can unwittingly and disproportionately limit their capacity to maintain their main pension saving through another scheme.[58]

The Office of Tax Simplification recommended that:

> The government should review the operation of the Money Purchase Annual Allowance, gathering better evidence, considering whether it meets its policy objectives, is set at the right level and is sufficiently understood, given the present potential for disproportionate outcomes.[59]

These concerns increased during the early stages of the Covid-19 pandemic when there were concerns that people accessing their pensions in response to a temporary drop in income would permanently reduce the amount they were able to save with tax relief in future. In February 2021, Yvonne Braun, the Director of Policy for Long-Term Savings and Protection at the Association of British Insurers said:

> Covid-19 has shown that households' financial resilience can be fragile and addressing that should be a central part of the nation's Covid-19 recovery. Our data suggests that pension withdrawals have not yet substantially increased but the continued uncertainty and insecure job market could mean more people dipping into their retirement savings to get by. Removing or increasing the Money Purchase Annual Allowance will help incentivise older workers to save. This will improve their financial resilience and also make sure people are not penalised for doing the right thing by paying money back into their pension when they can afford to.[60]

54 Reducing the money purchase annual allowance, HM Treasury, 23 November 2016

55 HM Treasury, Reducing the money purchase annual allowance, 23 November 2016; Taxation of Pensions Act 2014, Schedule 1, Part 4

56 Finance (No. 2) Act 2017 ;HM Treasury, Reducing the money purchase annual allowance, 23 November 2016

57 HM Revenue and Customs, Policy Paper: Pension Tax Limits, 15 March 2023

58 Office of Tax Simplification, Taxation and Life Events: Simplifying tax for individuals, October 2019, p12

59 As above, recommendation 9

60 Association of British Insurers, Scrap the Money Purchase Annual Allowance to help financial resilience, 26 February 2021

In February 2020, the Association of British Insurers also called on the Government to review the Money Purchase Annual Allowance, explaining:

> The MPAA, which effectively limits the amount of tax relief that can be received on contributions once the pot has been accessed, has also been a cause for concern. Its reduction to £4,000 means it affects individuals who continue to work but have accessed their pension, particularly as retirement is no longer a cliff edge. The MPAA disincentivises future saving permanently as the impact of a previous withdrawal cannot be reversed.[61]

Similarly, the Pensions and Lifetime Savings Association said in February 2021 that:

> At its current level of £4,000 per annum the PLSA feels that the MPAA has unintended consequences of limiting contributions from people who are in their 50s. For example, those people who may have been out of work though redundancy and found it necessary to dip into their pensions, who then go back into the workforce and are wanting to rebuild their pension pot rather than people who are purposefully 'recycling' their pension (which is the policy's intention). HMRC does not collect data on the number of people affected by the MPAA which makes it hard to evaluate its impact and to see if it is targeting the right people. The government should review the MPAA to ensure it is working as appropriately and is affecting the right people.[62]

Although HMRC does collect data on people contributing more than their annual allowance, it does not collect data on which annual allowance has been applies.[63]

2.4 Administering pension tax relief

There are two ways for employers to administer tax relief on pension contributions:

- Net pay: pension contributions are deducted from earnings before any tax has been paid. This means that tax relief is automatically given at the person's rate of income tax.[64]
- Relief at source: pension contributions are made after tax has been paid. Tax relief is claimed by the pension scheme at the relevant basic rate of income tax (20%).[65]

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61 Association of British Insurers, Five years on: Future-proofing the freedoms, February 2020, p23

62 The Pensions and Lifetime Savings Association, Five principles for pension taxation, February 2021

63 HMRC, Personal and stakeholder pensions statistics, 23 March 2022, notes to Table 7 and 8

64 Tax will be paid at the marginal rate, which is the rate of tax which would be paid on an additional pound of earnings.

65 The relevant rate of income tax is either the basic rate, the Scottish basic rate or the Welsh basic rate, all of which were 20% in 2022/23. For Scottish taxpayers paying no more than the Scottish starter rate HMRC does not recover the difference between the rate of income tax they pay (19%) and the relief they receive (20%). This is covered further in HMRC, Pensions Tax Manual, PTM044220 – Contributions: tax relief for members: methods: relief at source, 28 February 2022

Broadly, people paying the basic rate of income tax (20%) will receive the same tax relief under both arrangements. However, depending on the arrangement they are in, people who do not pay income tax and people who pay a higher rate of income tax may receive less tax relief than they are entitled to receive.

People with a marginal rate of income tax above 20%

People who pay more than 20% income tax still receive 20% tax relief in a relief at source arrangement. The additional tax relief they are entitled to can be claimed through a self-assessment tax return.[66] In a net pay arrangement, people who pay more than 20% income tax automatically receive tax relief at the correct rate of income tax.

People with a marginal rate of income tax below 20%

In a relief at source arrangement, someone who pays below the basic rate of income tax will still receive 20% tax relief on their pension contributions, up to the higher of £3,600 or their UK earnings.[67] For example, to contribute £100 to a pension scheme through relief at source, a person who does not pay income tax would contribute £80 from their earnings and the scheme would claim £20 from HMRC.

In a net pay arrangement, someone who does not pay income tax would receive no tax relief. To contribute £100 to a pension scheme through a net pay arrangement, a person who does not pay income tax would contribute £100 from their salary.

Government proposal

The Treasury published a response to a call for evidence in October 2021. It said it would proceed with "a variant of the bonus proposal".[68] It outlined the proposal for claiming bonuses (top-ups) as follows:

> 1. There will be no changes to how individuals save into pension schemes using [net pay arrangements] in 2024-25, with no change to take-home pay or pension contributions.
>
> 2. HMRC will make the necessary systems changes to enable identification of low earners in [net pay arrangement] schemes from April 2025, in respect of the 2024-25 tax year.
>
> 3. HMRC will calculate the amount of top-up any individual is entitled to, based on their pension contributions in 2024-25. This process will then continue each year from April 2026 onwards.
>
> 4. HMRC will notify individuals that they are eligible for a top-up and individuals will be invited to provide the necessary details for HMRC to be

66 Tax on your private pension contributions, Gov.uk [accessed 21 March 2023]
67 Finance Act 2004, section 190 and section 192
68 As above, para 2.31

able to make the payment to them. For those individuals that are digitally excluded, HMRC will provide additional support services to enable them to receive payment.[69]

An estimated 1.2 million low earners in net pay arrangements would receive an average top-up worth £53 in 2025-26.[70] The Government has said primary legislation will be required and it published draft legislation in July 2022 to be included in the 2023 Finance Bill.[71]

Further information is available in the Commons Library briefing Pension tax relief: The annual allowance and lifetime allowance.

2.5 Devolution of income tax rates

The Scotland Act 2012 introduced the Scottish rate of income tax from April 2016 and the Wales Act 2014 introduced the Welsh rate of income tax from 6 April 2019.[72] In Scotland, income tax rates now differ to the rest of the UK, which means that the tax relief received by Scottish taxpayers may also differ. The table below sets out the rates of income tax in 2022/23:

Table 1: Income tax rates

2022/23

Scotland			England, Wales and Northern Ireland		
	Band	Rate		Band	Rate
Starter Rate	£12,570 to £14,732	19%	Basic	£12,571 to £50,270	20%
Basic Rate	£14,733 to £25,688	20%	Higher	£50,271 to £150,000	40%
Intermediate	£25,689 to £43,662	21%	Additional	Over £150,000	45%
Higher	£43,663 to £150,000	41%			
Additional	Over £150,000	46%			

Source: Income tax policy proposal: Scottish Budget 2022-23, Scottish Government

Income tax personal allowance and the basic rate limit from 6 April 2022 to 5 April 2026, HMRC

This means there are additional differences between the tax relief provided through net pay arrangements and relief at source arrangements in Scotland.

Scottish taxpayers paying no more than the Scottish starter rate would receive 19% tax relief in a net pay arrangement and 20% in a relief at source scheme. For those in relief at source schemes HMRC has said it does not

69 HM Treasury, Pensions tax relief administration: Call for Evidence Response, October 2021, para 2.33
70 As above, para 2.34
71 HMRC, Policy Paper: Relief relating to net pay arrangements, 15 March 2023
72 Scotland Act 2012, sections 25-27, and Wales Act 2014, sections 8-11

recover the 1% difference between the rate of income tax (19%) and the rate of relief (20%).[73]

Like other people who pay more than 20% income tax, people paying the Scottish intermediate rate still receive 20% tax relief in a relief at source arrangement. They are able to claim the additional 1% they are entitled to through a self assessment tax return.[74] In a net pay arrangement, people paying the Scottish intermediate rate automatically receive tax relief at the correct rate.

In its response to its 2021 call for evidence on pension tax relief administration the Treasury said that it "is open to discussing the implications of this issue with the Scottish Government."[75] No further details have been published since then.

73 HMRC, Pensions Tax Manual, PTM044220 – Contributions: tax relief for members: methods: relief at source, 28 February 2022

74 Gov.uk, Tax on your private pension contributions [accessed 21 March 2023]

75 HM Treasury, Pensions tax relief administration: Call for Evidence Response, October 2021, para 2.35

3 What are the options for future reform?

3.1 Single rate of pensions tax relief

One option for reform is a single rate of tax relief, rather than relief being given at someone's marginal rate of tax. Those in favour of a single rate of pensions tax relief often argue that it would be fairer for all taxpayers to receive the same rate of relief. Under the current system higher rate income taxpayers receive a higher rate of pensions tax relief. Those opposed to a single rate of tax relief argue that it would be expensive to administer, unfair and inappropriately distort behaviour.

Advantages of a single rate of pensions tax relief

In 2005, the Pensions Commission, which was established to look at the adequacy of pension savings, said that a single rate of relief, described as a government "matching contribution", had significant attractions in principle:

> This proposal clearly has significant attractions in principle. It would improve rational incentives to save via pensions (individually or via employer contributions) for many lower income people who are currently accruing inadequate pensions. It would also make these incentives much clearer; people would be far more likely to understand the benefit offered.[76]

A report by the Pensions Policy Institute in June 2020 found that a flat rate of tax relief on defined contribution pension contributions would increase the proportion of tax relief going to basic rate taxpayers from 26% to 42%.[77] The Association of British Insurers, which sponsored the work, said that the pensions system needed to be changed so that it is "simpler, fairer to all earners and encourages saving for retirement.[78] In 2015, the Association of British Insurer's called for a single rate of relief – badged as a Savers' Bonus:

> A single rate will be easier to communicate than the current system, ensuring people understand the tax benefit of saving into a pension. It is well established that matching contributions are the most effective incentive for increasing pension participation and contribution rates, as loss aversion means people save so as not to miss out on them. Following the example of the

76 Pensions Commission, A New Pension Settlement for the Twenty-First Century; The Second Report of the Pensions Commission, November 2005, p318

77 Pensions Policy Institute, Tax relief on Defined Contribution pension contributions: PPI Briefing Note number 122, June 2020

78 Association of British Insurers, Low earners missing out on vital tax relief despite more saving for a pension, 23 June 2020

> Automatic Enrolment advertising to make the Savers' Bonus as visible at the matched employer's contribution could therefore have a powerful impact.[79]

This approach was supported by the Low Incomes Tax Reform Group, which argued that a single rate of tax relief would improve incentives for those on low incomes:

> [The Low Incomes Tax Reform Group] therefore proposed a standard rate of tax relief for all of 33.3% in order to incentivise those on low incomes in particular to set aside money for later years and possibly a top-up at age 30 to encourage an early start to the savings habit, vital to accumulate the pension pot needed to support maybe 30 years of post-employment life. The competing demands of starting work at the bottom of the salary scale, repaying student loans, saving for the deposit for a house and starting a family make saving for the far-distant years of retirement a low priority and in many cases an impossibility when there simply is no spare money after the basic bills have been paid.[80]

And that could simplify aspects of the system:

> Doubtless Governments would be keen to apply an annual cap to avoid an open-ended drain on the public purse [...] The connection, however, between the amount contributed and the state top-up would be much clearer if annual statements showed savers' contributions and Government additions separately and in aggregate. [...] It would also render unnecessary the complex structure of lifetime allowances, annual allowances, tapering allowances, individual protection and the uncertainty of the ultimate valuation of both DB & DC pensions pots.[81]

Issues with a single rate of tax relief

A single rate of tax relief, unless accompanied by further measures, could mean double taxation for higher rate taxpayers. Higher rate taxpayers might first be expected to pay tax on the difference between their marginal rate of income tax and the flat rate of tax when making contributions. When those savings are withdrawn as a pension, under the current system, income tax would again need to be paid.

The Pensions and Lifetime Savings Association looked at three options for a single rate of relief in a 2021 report. It found that:

- A single rate at 20% would result in double taxation for higher earners who pay a reduced rate of tax when they make pension contributions and income tax when they withdraw their savings.
- A single rate at 25-30% would "improve adequacy" for basic rate taxpayers though there would be a negative impact on higher rate taxpayers who could still be double taxed on their pensions.

79 Association of British Insurers, A Savers Bonus (PDF), October 2015

80 The Low Incomes Tax Reform Group, Strengthening incentives to save for pensions, 29 October 2015

81 As above

- Continuing the current regime for defined benefit schemes and introducing a single rate for defined contribution schemes would improve adequacy for basic rate taxpayers but have a negative impact on higher rate taxpayers.[82]

The Pensions and Lifetime Savings Association found that none of the three single rate options it considered were simple to adopt and administer.[83] It also said that there would be additional complexities for defined benefit schemes where contributions are more complicated to measure which would involve annual calculations and repayments for every higher rate taxpayer.[84]

The Institute for Fiscal Studies said that one option could be for there to be a uniform rate of relief on contributions and uniform rate of tax on pension income. However, it said it was debatable whether this would be an improvement and there would be a "major practical difficulty in restricting the rate of relief".[85]

Cost to the Government of introducing a flat rate of relief

The level a flat rate of pensions tax relief was set would determine how much it would cost the government compared to the current system. In June 2020, the Pensions Policy Institute estimated that a 20% flat rate would cost £5.8 billion and a 33% flat rate would cost £9.6 billion, compared to a cost of the current system of £9.3 billion.[86]

In its 2016 Green Budget, the Institute for Fiscal Studies said that the impact on revenues in the longer term was more uncertain:

> If lower- and middle-income individuals end up having larger pension pots (for example, because they choose to save more or just because of the higher amount of up-front tax relief), then tax revenue on the resulting pension would increase. But if higher-income individuals end up having smaller pension pots (due to them saving less or just because they received less up-front tax relief), then this would result in less tax revenue on the resulting pension. Any impact on household saving and spending decisions would also impact upon future indirect tax revenues.[87]

82 The Pensions and Lifetime Savings Association, Five principles for pension taxation, February 2021
83 As above
84 As above
85 Institute for Fiscal Studies What are the options for reforming pensions taxation?, [accessed 21 March 2023]
86 Pensions Policy Institute, Tax relief on Defined Contribution pension contributions: PPI Briefing Note number 122, June 2020
87 Institute for Fiscal Studies, Green Budget 2016, February 2016, p119

3.2 Taxing pension contributions

In the UK, private pension saving is taxed on an "exempt, exempt, taxed" model (EET). This means that tax is not paid on contributions and investment growth, but tax is paid when savings are used to make pension payments. A different approach which has been considered is a "taxed, exempt, exempt" model (TEE). In this system contributions are taxed like other salary and no tax is paid on investment growth and payments from savings. In 2020, the OECD reported that Costa Rica, Czech Republic, Hungary, Israel, Lithuania, Luxembourg, and Mexico, were all using variants of a taxed, exempt, exempt model.[88]

In 2015, the Treasury described a system where contributions are taxed upfront and then topped up by the government. The Treasury said:

> [...] this may allow individuals to better understand the benefits of contributing to their pension as the government's contribution might be more transparent, and they would no longer need to consider the future tax implications of their pension choices or work out how much their pension pot is worth given their expected tax rate in retirement. Equally, others have argued that the current system, where no tax is due on pension contributions while working but tax is paid in retirement, is simple for individuals to understand and also provides an incentive to leave money in their pension pot.[89]

Reform along these lines had been proposed by the Centre for Policy Studies in 2014, which said that the current tax-based incentives for pension saving were expensive, had failed to stimulate a broad-based retirement savings culture and represented a "huge subsidy for the pensions industry". The Centre for Policy studies proposals include replacing tax relief with a Treasury contribution of 50p per £1 saved up to an annual allowance.[90]

Impact of moving to a new system

In July 2021, the Pensions and Lifetime Savings Association published a discussion paper outlining five principles for pension taxation. It looked at a system where "income tax is full applied to all contributions but investment returns and income in retirement are both exempt from tax". It found that this would not promote adequacy or encourage the right behaviours, because it disincentives pension savings and that changing the current system would mean "a two-track system will have to be supported potentially for decades."[91]

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88 OECD, Financial incentives for funded private pension plans: OECD country profiles 2021, 3 December 2021

89 HM Treasury, Strengthening the incentive to save: a consultation on pensions tax relief, Cm 9102, July 2015, para 3.12

90 Centre for Policy Studies, Retirement savings incentives: the end of tax relief and a new beginning, 2014

91 The Pensions and Lifetime Savings Association, Five principles for pension taxation, February 2021, p14-15

The Association of British Insurers was concerned that that the transition to the new system would be complex, as for the foreseeable future anyone who already had pension savings would have a "confusing mixture of taxed and untaxed pension income when they come to retire".[92] In 2015 it said:

> A move to a TEE system for pensions would be both very costly and time consuming to implement. For pension providers alone, costs are likely to be in the hundreds of millions for the system changes necessary for employers, payroll providers and the pensions industry are such that the implementation timeline would risk stretching over two parliaments.
>
> More concerned than the build cost is the creation of EET legacy system which will need to be serviced for decades. For example, a 22-year old who already has a workplace pension through AE would open an additional pension account under TEE, and both would run in parallel until their retirement.[93]

Impact on retirement incomes

The impact on pension incomes would depend on the details of a new system and whether or not the government makes payments to top up pension saving. In 2015, analysis by the Pensions Policy Institute found that:

> A pure TEE system without matching contributions is likely to reduce pension outcomes, because, with tax being paid up front, none of the pension is received tax free, and the tax paid is at the individual's marginal rate in work, rather than an average rate after retirement.
>
> Giving a matching contribution on a TEE system is similar to a flat rate EET system in the accumulation phase.
>
> A TEE system with significant matching contributions could increase the outcomes for individuals.[94]

In July 2021, the Pensions and Lifetime Savings Association said that a move from EET to TEE would "negatively impact adequacy as it removes all tax benefits, disincentives saving into pensions, reduces the amount being saved and, will result in lower incomes in retirement." [95]

The Association of British Insurers argued that the change would undermine responsible saving, saying that:

> The current system acts as a brake against people spending their entire pot early in retirement. This is because there is an incentive to spread income over multiple years to reduce the amount of tax payable. Without such a brake, people will be tempted to withdraw all their money as soon as they can, to keep it 'safe', risking poor investment decisions that will reduce the value of their pension and make them more reliant on state support in later life. This tendency will be exacerbated if people perceive the need to keep their money

92 Association of British Insurers, A Savers' Bonus, October 2015

93 Association of British Insurers, A Savers' Bonus, October 2015

94 Pensions Policy Institute, Comparison of pension outcomes under EET and TEE tax treatment, October 2015

95 The Pensions and Lifetime Savings Association, Five principles for pension taxation, February 2021

> safe from future administrations that might decide to tax pensions in payment.[96]

Impact on tax and Government spending

In its 2016 Green Budget, the Institute for Fiscal Studies argued that moving to TEE tax treatment has "much more dramatic consequences for the profile of tax revenues and poses significant political risks". It said that:

> Moving to a system in which contributions are taxed up front rather than on receipt would dramatically boost tax revenues in the near term. But levying this income tax up front would come at the expense of a reduction in revenues in the future, as the government will no longer collect income tax on these pensions in payment. [97]

It explained that the longer run cost would depend on the size of any new tax incentives and explained:

> The government estimates that up-front income tax relief on pension contributions totalled £27.0 billion (£6.8 billion on individual contributions and £20.2 billion on employer contributions) in 2013–14. However, much of this will be recouped in future from income tax received when private pension incomes are drawn. In 2013–14, £13.1 billion of income tax was paid on income received from private pensions. This figure gives some feel for how much of the up-front tax relief might be only temporary, though in practice future growth in the pensioner population is likely to push this number up. If the government also wanted to introduce a significant up-front top-up, then it would be quite possible that the vast majority of any additional income tax revenues raised in the short term would be temporary rather than permanent.[98]

In July 2021, the Pensions and Lifetime Savings Association said that a move from EET to TEE "could lead to an upfront positive fiscal flow for [the Government], the revenue gain would fall over time as income from pensions in payment fall and then stop."[99]

3.3 Reforming pension tax relief and National Insurance Contributions (NICs)

National Insurance Contributions (NICs) are normally deducted from an employee's earnings before their pension contribution. This effectively means that employee NICs are charged on pension contributions but no NICs are charged on pension income – a "taxed, exempt, exempt" model.

NICs are not taken from an employer's contribution to an employee's pension – an "exempt, exempt, exempt" model. Some employers use salary sacrifice

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96 Association of British Insurers, A Savers' Bonus, October 2015

97 Institute for Fiscal Studies, Green Budget 2016, 8 February 2016, p119-20

98 As above

99 The Pensions and Lifetime Savings Association, Five principles for pension taxation, February 2021

schemes, where an employee receives a lower salary which is compensated by the employer making a larger contribution to the pension scheme without paying NICs.[100]

The Institute for Fiscal Studies, a UK economics research institute, has proposed that employee NICs should align with the pension tax relief approach for income tax and move to an "exempt, exempt, taxed" model, with pension income, rather than contributions, being subject to employee NICs.[101]

It also proposes that employer contributions should be moved to a "taxed, exempt, exempt" model to "end the current state of affairs whereby the effective subsidy on pension contributions is arbitrarily altered whenever the employer NICs rate changes and ensure a uniform incentive for all employers".[102] It has suggested that a employers receive tax relief in the form of a subsidy for their pension contributions instead.

3.4 2015 Treasury consultation on reforming pension tax relief

The case for change

In July 2015, the Government launched a consultation on reforming pension tax. Its objectives were to improve incentives and contain costs:

> Longevity has also changed the way that pensions are provided. In the private sector, employers are now less likely to offer a defined benefit pension scheme to new employees and instead are frequently turning to defined contribution pensions. This has changed the way that the pensions industry is structured and consumer expectations of how pensions should be provided.
>
> [...]
>
> Increasing longevity and changes in pension provision therefore provide the context for considering whether there is a case for reforming pensions tax relief. As our society continues to age, it will become increasingly important for government to ensure that all individuals are supported to save for their retirement by offering clear, simple and transparent incentives. However, in the context of the deficit and the continuing press on public finances, it will also be important to ensure that this support is sustainable for the longer term. [103]

On incentives, the Government cited research by the Pensions Policy Institute suggesting that "for lower income groups tax relief is not an important

[100] MoneyHelper, Salary sacrifice and your pension [accessed 15 March 2023]
[101] Institute for Fiscal Studies, A blueprint for a better tax treatment of pensions, February 2023
[102] As above
[103] HM Treasury, Strengthening the incentive to save: a consultation on pensions tax relief, Cm 9102, July 2015, Foreword

determinant in people's decision to save." Trends in workplace pension saving made it increasingly important to ensure the right incentives were in place. This is because auto-enrolment is increasing the numbers saving in a pension.[104] However, the majority are being auto-enrolled into a defined contribution scheme, increasing the importance of ensuring they are contributing enough to achieve an adequate income in retirement. [105] DWP analysis in 2014 suggested that almost half of adults below State Pension age were not saving enough for their retirement.[106]

A 2013 report from the Pensions Policy Institute found that the evidence around the effectiveness of tax relief as an incentive was limited. It noted that issues included:

- Lack of understanding around tax relief.
- People redirect money from savings into a pension, rather than increase their savings overall.
- Higher earners, who may be more likely to save, are more likely to respond to incentives.
- Tax relief has not led to enough saving to close the 'Savings Gap'. [107]

More general barriers to pension saving included:

- People have insufficient income to make pension savings.
- Lack of understanding around pensions.
- Issues related to the current design and delivery of pensions.
- Inertia.[108]

In its response to the 2015 consultation, the Pensions Policy Institute argued that a large fiscal incentive was not necessarily enough in itself to change behaviour. However, if an incentive was not easily understood, individuals would not be able to respond to it. There was some evidence that matching contributions affected behaviour:

> There is some evidence to suggest that such matching contributions do affect behaviour, in the context of US pension saving and in other savings policy areas in the UK. This might be easier with a single rate of matching than, for example, in the current system where the match depends on the tax band of the individual. Presenting the current system as a match could also lead to

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104 Further information on automatic enrolment is available in the Commons Library briefing SN 06417 Pensions: Automatic enrolment - current issues

105 HM Treasury, Strengthening the incentive to save: a consultation on pensions tax relief, Cm 9102, July 2015, para 1.24; Department for Work and Pensions, Scenario analysis of future pension incomes, August 2014

106 Department for Work and Pensions, Scenario analysis of future pension incomes, August 2014

107 As above, p24

108 As above, p24

questions as to why higher earners receive a higher match, and the technical explanations might be hard to get across to individuals.[109]

The Pensions and Lifetime Savings Association, previously the National Association of Pension Funds (NAPF), argued that looking at tax relief in isolation could be counter-productive and that the Government should focus on auto-enrolment. It said that "over the long term, a move to a pensions tax regime of either 'taxed, exempt, exempt' (TEE) or a single rate jeopardises both pension saving and the tax revenues of future governments."[110]

Response - Budget 2016

In Budget 2016, the then Chancellor did not announce any fundamental change to the tax treatment of pension on the grounds that there was 'no consensus'.[111]

The then Chancellor did announce the introduction of the Lifetime ISA to encourage saving into for house purchase or retirement. The background to the introduction if the Lifetime ISA is discussed in the November 2016 Commons Library briefing Lifetime ISA and pensions.

Response were mixed. The Pension and Lifetime Savings Association, for example, described "no change" as the right decision.[112] However, Mick McAteer of the Financial Inclusion Centre said it was disappointing that the Government had stepped away from "the clear inequality in our pension system."[113] Dot Gibson of the National Pensioners Convention agreed, saying the Chancellor had "wasted a golden opportunity to not only reform the unfair system of pension tax relief".[114]

109 Pensions Policy Institute, Response to HM Treasury consultation: strengthening the incentive to save, October 2015
110 Pensions and Lifetime Savings Association, Strengthening the incentive to save: a consultation response on tax relief, October 2015
111 HC Deb 16 March 2016 c96
112 Pensions and Lifetime Savings Association, Pensions and Lifetime Savings Association comments on Budget 2016, 16 March 2016
113 'Osborne scraps pension tax relief shake-up', Financial Times, 6 March 2016
114 Pensions: George Osborne drops plans to cut tax relief, BBC News, 5 March 2016