

## ABI consultation on annual allowance consultation – 27 August 2010

### Summary of ABI's consultation response

- The ABI has today submitted its response to the HMT consultation on higher rate tax relief for pension contributions (deadline - Friday 27<sup>th</sup> August.)
- The ABI feels an annual allowance of £45,000 will keep the maximum number of people as possible saving into a pension. Our modelling shows this can still raise the revenues the Government needs. The Treasury consultation suggests a range between £30,000 to £45,000.
- We believe a limit below £35,000 is unworkable. It would require too many exemptions and fail to restore the simplicity needed to rebuild consumer confidence in pensions.
- We do not support proposals to reduce the lifetime allowance or cap pensions tax relief at 40%. This will introduce even more complexity into the pension system.

### Quote

Maggie Craig, the ABI's acting Director General, said:

"The Government are right to simplify the pension tax system. It will help consumers understand the benefits of saving, and help tackle the chronic under-saving we face.

"However, it is crucial that this good work is not undone by setting an annual limit at an unworkably low level. It needs to work for a range of individual circumstances so that consumers can have the greatest control over how they save towards their retirement.

"The new rules must also avoid new complexity, through reducing the lifetime allowance or capping relief at 40%."

### Key points of ABI consultation response on the annual allowance

- The annual allowance must be set at a level high enough to work for consumers and for the pensions industry. The limit should be set at a level that encourages a wide range of savers and that for the industry will be broadly revenue neutral. **The £45,000 limit we have suggested** would be optimal in incentivising saving to as many people as possible.
- The insurance industry **welcomes the simpler approach** proposed in the emergency Budget to changes on tax relief on pension contributions. The consultation document published by HMT supports our earlier proposal for an annual contribution ceiling individuals could pay into their pension and receive tax relief at their marginal rate of income tax.
- An annual allowance will be **easier for savers to understand**, keep higher levels of engagement with pensions and reduce the significant administration burdens and their associated costs. It will also **keep those responsible for making decisions** on staff pension schemes engaged. They would be much less inclined to support staff pensions if they no longer benefited from tax relief at the marginal rate.
- Exemptions from the limit should be kept to a minimum but mitigation of tax charges in some contexts is vital to ensure fairness, in particular, **modest earners who acquire increased benefits in defined benefit pensions because of illness or redundancy should be protected**.
- There will be very little time to make the required changes to literature, systems etc. It is therefore **important that draft legislation is produced as early as possible** and that

interested parties are kept fully informed of any changes as the draft legislation progresses to final.

- Unlike the previous proposals, **an annual allowance keeps the principle of deferred taxation largely intact**. People will pay tax on income in retirement and relief at source just relieves them of the tax they have already paid via income tax so they are not taxed twice. It is in society's interest to encourage this so as many people as possible have viable pension pots in the future and are not reliant on the state.
- An annual allowance cap is **simple, easy to understand** and an easy to sell proposition which is desperately needed after the mind-boggling complexity introduced into the system.

#### **Other points from ABI consultation response**

- **We do not favour any reduction in the lifetime allowance**. The change is unnecessary, the low annual allowance naturally limits the amount people can build up in their pension. Further change undermines consumer confidence in the stability and predictability of pensions, adds further complexity and increase admin costs.
- Similarly, **capping the rate of relief at 40% will also undermine both the simplicity and predictability of the pension system**.

#### **Background information**

- The Emergency Budget committed the Coalition Government to review relief for pension contributions with a view to restricting tax relief from 6 April 2011. A reduction in the annual allowance (to a range of £30,000- £45,000) was proposed but subject to further consultation.
- The original changes by the last Government were: From 2011, those earning over £150,000 will see their pension tax relief gradually eroded from 50 per cent to 20 per cent for earnings of £180,000 or more.
- The current annual allowance for pension contributions is £255,000.