PENSIONS POLITICS OPINION

Ros Altmann: It has never been more important for government to leave pensions alone

Instead of attacking pensions with short-term cost cutting, the chancellor should call on schemes' long-term assets to 'Build back better'

By **Ros Altmann** | 12th August 2021 8:00 am

Pension assets worth well over £2trn are a source of long-term domestic savings to help with much needed investment to boost growth, as well as address huge risks from climate change.

I am therefore disappointed by more rumours of a tax raid on pensions as the Treasury seeks huge sums to help fund the pandemic costs. One day, no doubt, there will be major reform of the £50bn annual spending on tax and National Insurance (NI) pension reliefs, but I do hope not now.

Tinkering with incentive structures for pensions can have serious consequences, risking a rise in old-age poverty and depleting national resources for infrastructure, housing and small-business development.

> Lowering the LTA adds to intergenerational unfairness

Our pension system rests on the principle of a very low basic state pension, supplemented by private pensions with taxpayer-funded incentives, plus employer payments, to provide better retirement incomes.

Lesser of three evils?

Three reforms reportedly are in chancellor Rishi Sunak's sights:

- Cutting the lifetime allowance (LTA) to around £800,000
- Removing higher-rate pensions tax relief
- Reducing employer reliefs.

Each of these has major drawbacks.

I can feel readers' eyes rolling at the thought of yet another change to the LTA. The most sensible reform would be to scrap it altogether.

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The 2006 original £1.5m limit has moved up and down more than the Grand Old Duke of York. It rose to £1.8m in 2010, reduced to £1.5m, £1.25m and finally £1m by 2016, before rising to £1.073m in 2019. At the last Budget it was frozen.

This yo-yoing makes a mockery of long-term pension planning. Defined contribution (DC) funds rely on strong investment performance. With annual contributions already limited, it makes no sense to punish long-term investment success with 55% penal tax charges.

> Tinkering with a few parts of the system risks profound and multifaceted ripple effects

The LTA is bad policy for both DC and defined benefit (DB) schemes. It already incentivises NHS and other public-sector staff to retire early to avoid the tax, and this would increase with lower limits.

Lowering the LTA also adds to intergenerational unfairness. Many older people have protected higher LTAs, so reducing it hits just younger people and those who did not earn huge sums early in their career.

What about removing higher-rate tax relief? There are social policy justifications for giving everyone who puts money into their pension the same taxpayer incentive, but there would be an outcry from those earning over £50,000 who get at least £2 for every £3 they contribute.

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Removing higher-rate relief sounds appealing but becomes far less attractive on closer inspection. It would create significant difficulties for traditional DB schemes, which comprise the majority of tax relief costs; and, of course, changing reliefs just for DC schemes would be inequitable.

The third suggestion of limiting tax relief for employer workplace contributions may also have short-term cost-saving benefits for the Exchequer. However, it has problematic side-effects too, such as driving more employers to reduce pension contributions to minimum levels and undermining salary-sacrifice arrangements, leaving millions poorer in retirement.

Employer holidays

A more effective short-term cost-saving measure may be to encourage DB scheme employer pension contribution holidays for a year or two, to promote post-Covid recovery and improve corporate strength while saving billions in tax relief on contributions.

I encourage the chancellor, rather than attacking pensions, to use the long-term assets to 'Build back better', improve green growth, promote social housing and boost the economy directly.

> The LTA is bad policy for both DC and DB schemes

The major pension tax relief review in 2015 highlighted how radical reforms required in-depth consideration of the broader pensions landscape. Tinkering with a few parts of the system in pursuit of near-term cost cutting