ECONOMY FINANCIAL EDUCATION INVESTMENTS PENSIONS REGULATION MM WEEKEND ESSAY

Weekend Essay: Is it too late to fix a broken pensions system?

By **Michael Klimes** | 7th May 2021 3:00 pm

Tweets are not known for their factual accuracy or eloquence of expression. This is especially true when they come from the brain of a former US president. So, it is a charming surprise when you encounter one that resonates with you.

I had this experience when I read a tweet by pensions expert Helen Morrissey from Royal London about the UK's pension system. It said: "Just been reminded by @RayVay [Rachel Vahey] that yesterday was the 15th anniversary of A-Day – otherwise known as pension simplification – how is that going do you think?"

The observation inspired wry responses from other experts in the pensions sector about 6 April 2006. That is an infamous date as it is when 'pensions simplification' took effect. The ironic title hides the mind-numbing complexity introduced by the dour Scotsman who goes by the name of Gordon Brown.

The changes announced in the 2004 Budget streamlined eight different pension tax regimes into one. They also introduced the annual and lifetime allowances to ensure all get their fair share of tax relief. These two policies have been particularly divisive among the IFA community as the amount a client can save in either has been slashed over the years.

When introduced in 2006 the limits were £215,000 and £1.5m, respectively but now stand at £40,000 and £1,073,100. Many commentators question whether both are even needed.

While it is tempting to blame Brown for all the fun it fails to acknowledge the truth that successive chancellors have meddled too. Speculation before every budget in the last 14 years has persisted whether the government is Tory, Labour or a coalition government.

Politicians view pensions as either a quiet way to generate tax revenue or a quick way to win votes. That creates a fundamental tension with what pensions are supposed to do: generate an income in retirement.

The expediency creates a long and distinguished list of adverse consequences for all savers. What is striking is the sheer range of taxpayers caught out by all the tinkering.

Take the low-paid. Everyone seems to agree the pandemic has revealed how undervalued key workers are. Many in the media are beating the drum for those such as social carers to be paid more and assigned greater respect. An area of public policy that could be looked at is pensions.

One of the real triumphs of pension policy since 2000 is the establishment of auto-enrolment. The introduction of compulsory saving in workplace schemes has led to tens of millions saving who previously would not have. But kinks in the system remain and it is hard to understand why they are not resolved. A glaring issue is the employers who choose an auto-enrolment scheme administered on a net pay basis.

Such schemes cannot add the 25% bonus of tax relief to contributions of workers earning less than £12,500 a year from the employer. It is fair to presume some social carers fall under this threshold. A brief Google search shows former pensions minister Baroness Ros Altmann has written about the problem for *Money Marketing* since at least July 2017. She has returned to the subject on several occasions in other columns, but nothing gets done. If a well-connected and established peer cannot move the dial, what hope is there for the rest of us?

The problem is of sufficient gravity to be mentioned in the Conservative election manifesto for the 2019 election. It reads: "A number of workers, disproportionately women, who earn between £10,000 and £12,500 have been missing out on pension benefits because of a loophole affecting people with net pay pension schemes. We will conduct a comprehensive review to look at how to fix this issue."

Although a global pandemic is underway the absence of any policy to correct the fault in the last budget attracted much comment. These significant problems also effect the highest rate taxpayers. NHS consultants and doctors have been caught out by several wretched allowances. The holy trinity are the annual allowance, tapered annual allowance and money purchase annual allowance.

I remember the headache trying to understand how all it works gave me. Fortunately, the British Medical Association has plain English that diagnoses the maladies for us:

“If your threshold income is above £200,000 and your adjusted income is below £240,000 you will be subject to the standard annual allowance.

“If your threshold income is above £200,000 and your adjusted income is above £240,000 then your annual allowance will be reduced. For each £2 that your adjusted income exceeds £240,000, your annual allowance threshold is reduced by £1. If your adjusted income exceeds £312,000 or over then you will have a reduced annual allowance of £4,000 only.”

No matter how many times I read that passage I become confused and perhaps the same is true for doctors or consultants. These are not the least educated or intelligent people you can meet in the population.

Apart from allowances short term pensions reform has encouraged some of the worst phrasemaking in the English language. Try and get your tongue around uncrystallised funds pension lump sum or its ghastly acronym UFPLS. News reporting is meant to have succinct language in the headline and opening paragraph. We do that to attract the reader and I wonder how I have survived with such a mouthful to digest over the years?

Of course Gordon Brown is not to be blamed for all the blather as George Osborne has to take some credit. He introduced the pension freedoms in 2014 and enjoyed his own cleverness as much as Brown. It's a shame I could not enjoy the cleverness as much as Gideon did. The number of income thresholds and unforeseen tax traps is as numerous as Osborne's jobs.

The only number that is greater than the number of Osborne's jobs or allowances is the quantity of pension ministers. The majority are lucky if they last a year as the brief is tough and is helped by knowledge of the subject. The two most impressive in my six and a half years as a pensions reporter are Steve Webb and Guy Opperman.

A major factor in their effectiveness has been the fact they were in the role long enough to make substantial change. Webb brought in the the single tier state pension and the incumbent Opperman has got solid legislation through parliament.

The Pension Schemes Act legislates for the creation of pensions dashboards that should allow members to see all their retirement pots in one place.

It also gives trustees power to restrict the statutory right to transfer if they suspect suspicious scams activity. Although widely welcomed the rules are retrospective in the sense that they follow the unintended consequences of radical deregulation. The same is true of a raft of FCA rules designed to clear up the defined benefit transfer market such as the contingent charge ban. Clearly longer-term thinking is needed to give the country the pensions system it needs.

The model repeatedly invoked is the pensions commission that found the political will and consensus for auto-enrolment. It was bipartisan and took a detached and technocratic approach to under saving among the public.

Could a similar approach work again?

You might think the answer is no as the idea of a pensions commission has been aired repeatedly by thinktanks and commentators. It only seems to have consistent support among those who make a living from pensions, in other words the pensions industry. The vast majority of MPs are too busy with the immediate needs of their constituents or more focused on glamorous topics such as foreign affairs.

There is also the eternal conundrum of democratic politics that sees difficult subjects like pensions or social care avoided due to the five-year electoral cycle. If you can't win votes from the topic, why mention it at all? Look at what happened to Theresa May on social care during the 2017 election. Headlines in the Daily Mail torpedoed her chances of securing a decisive majority she desperately wanted.

You can have no sympathy whatsoever for Boris Johnson and grasp why headlines on the triple lock make him nervous: it's a potential hornets' nest waiting to blow up and sting him in the face. Even though many policy wonks talk about the unfairness the triple lock places on the younger generations, meaningful reform is unlikely. The same goes for moving to a flat rate of tax relief: too many voters will be upset in the process.

It is also one area where the interests of politicians and the pensions industry converge. The Pensions and Lifetime Savings Association has spoken against rocking the boat on tax relief and maintaining the status quo.

Then again, we are living in "unprecedented times" as the mantra goes with constant rhetoric about "building back better". I do want to believe in such noble aspirations but the last year and experience more generally has taught me two things: try to live in the moment and believe it when you see it.

Who would have thought a majority Tory government would have paid the salary of millions of private sector workers 14 months ago? Who would have thought the government that botched the handling of the pandemic so badly would have one of the best vaccine programmes in the world?

The only certainty in life is change and that is especially true in the world of Covid-19. Politicians don't know the future anymore more than we do and that makes the likelihood of more tinkering of the pensions system greater.

That does not please seasoned pensions watchers like me as I have to re-learn how all the allowances work. This gives me a headache and I am sure advisers, and their clients share my pain.

Luckily, I have the great and good of the pensions industry to help me understand what is going on through their eloquent commentary. Any new jargon that is bound to emerge will be as weird as a former US president's tweets.

By **Michael Klimes** | 7th May 2021 3:00 pm