2018 Budget Representation

To: HM Treasury **By:** The Intergenerational Foundation **Date:** 6 February 2020

The Intergenerational Foundation (www.if.org.uk) is an independent think tank researching fairness between generations. IF believes policy should be fair to all – the old, the young and those to come.

1. Introduction

1.1 The Intergenerational Foundation (IF) strongly believes that the interests of younger and future generations are being neglected in current government policy, and calls for reforms that address the growing imbalances between the generations. Our research agenda spans a number of different policy areas for which our recommendations have been set out below:

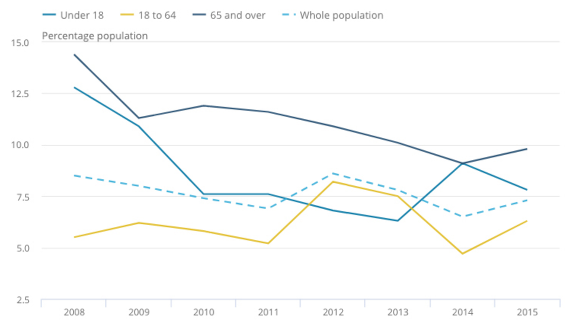
2. Levy National Insurance (NICs) on working over-65s

2.1 There are 1.2 million people over 65 years of age still working.[1] Far from being poorer people, three-quarters of these working people are higher-paid professionals who remain in the same job after reaching State Pension Age (SPA).[2] Giving tax relief in this way to the over-65s implies that the general (younger) taxpayer will have to be taxed more heavily to make up the difference. This means that the removal of NICs functions simply as a pay rise for the vast majority of people in this position, which is delivered at the expense of other workers.

2.2 NICs made by employers for each employee are still levied at the same rate regardless of whether the worker is above state pension age or not, which seems inconsistent with the contributory principle argument which goes that contributions should stop once retirement age has been reached.

2.3 The over-65 population is no longer poorer than other generations (see Figure 15, ONS). According to Age UK, poverty levels are half what they were 20 years ago, with two million (16%) of pensioners in the UK living in poverty in 2018.[3] This is a smaller amount (as both a proportion and an absolute number) than among children.

Figure 15: Persistent poverty rate by age group, 2008 to 2015, UK



Source: Office for National Statistics, Eurostat

[1] ONS (2018): https://www.ons.gov.uk/peoplepopulationandcommunity/birthsdeathsandmarriages/ageing/articles/livinglongerhowourpopulationischangingandwhyitmatters/2018-08-13

[2] Smeaton, D. and McKay, S. (2003) Working after State Pension Age: Quantitative Analysis, London: Department for Work and Pensions

[3] Age UK (2019) https://www.ageuk.org.uk/globalassets/age-uk/documents/reports-and-publications/reports-and-briefings/money-matters/poverty_in_later_life_briefing_2019.pdf

2.4 The Child Poverty Action Group (CPAG) estimates that there were **4.1 million children** living in poverty in the UK in 2017-18, which equates to 30% of children.[4]

2.4 A group of Conservative MPs from the Free Enterprise Group has estimated **that £2 billion could be raised from levying NICS on over-65s**. Such a sum could help offset the cost of caring for Britain's rapidly ageing population.

3. Limit pension relief on the 25% tax-free lump sum

3.1 Pensioners are able to take a tax-free "lump sum" out of their private pension saving when they begin drawing their pension that can be worth up to 25% of the total value of the fund. This is an extremely regressive and unfair form of tax relief, for the following reasons:

1) It gives more away to wealthier pensioners

It stands to reason that wealthier people are likely to have more valuable private pension savings. Therefore, the fact that the amount which they can take out of their pension fund tax-free is calculated as a percentage of the fund's value means that wealthier pensioners get more out of this tax subsidy than poorer ones, making it socially regressive.

2) It undermines the point of pension saving

The whole idea behind incentivising people to save money into pensions is that it should result in them having more resources in retirement, meaning they should be less of a burden upon the state during their later years. However, allowing people to take a quarter of the value of their pension fund as a lump sum completely undermines these aims because it encourages people to spend down a large chunk of their resources at the beginning of their retirement, rather than smoothing out the amount which they have saved across the whole period, as they would do if they bought a more generous annuity product instead.

3) It increases costs for the state

Pensioners who withdraw a large chunk of their accumulated pension savings up-front as a lump sum will end up with a lower pension income because they will have less money remaining in the fund to be converted into an annuity. Its value will decrease still further if they do not purchase inflation protection. Therefore, the tax-free lump sum increases the risk of individuals needing to access means-tested benefits at some point during their retirement, creating higher costs for the state which are borne by younger generations.

3.2 Potential Revenue: Rising from very little to £9.2 billion per annum in the future

There are a variety of different ways in which the tax relief on pension lump sums could be curtailed. One obvious strategy for increasing the degree of fairness within the system would be to cap the amount that can be claimed tax-free in cash terms. The Pensions Policy Institute suggested imposing a cap of £36,000. A more radical step would be to abolish the tax-free lump sum completely by gradually phasing it out over a period of years. The think tank Centre Forum have suggested that this could be achieved by imposing a cap on lump sums for people who already have private pension savings and not allowing further accrual towards the cap for people whose current pension savings are below the capped level. As people would have an incentive to stop taking lump sums altogether, the main benefits of this policy would gradually be felt over years to come as people substitute their lump sums for purchasing more generous annuities, which would give them a higher taxable income in retirement. The authors estimate that this could eventually deliver annual revenues of £9.2 billion in the future, although the initial gains would be very small.

4. Reduce interest rates on Student loans

4.1 Stop charging students interest of RPI plus up to 3% (which means students enrolling at English universities this year will pay 6.4% interest while they are still studying) when this is substantially higher

[4] Child Poverty Action Group (2019): https://cpag.org.uk/child-poverty/child-poverty-facts-and-figures

than the interest rate on government gilts (i.e. the cost to the government of borrowing the money that they are then lending back out again to the students), which is around 2.5%. Interest on student loans could be reduced by changing the measure of inflation used to calculate the rate of interest from the Retail Prices Index (RPI) to the Consumer Prices Index (CPI), which would also be fairer because this is widely considered to be a more accurate measure of inflation

4.2 There is no justification for charging students the extra 3% when this is supposed to be means-tested on the basis of their earnings and they haven't started working full-time yet.

4.3 Give every student and graduate the ability to view exactly how much they currently owe, how much interest they are being charged and the amount they have currently repaid in real time through the Student Loans Company website.

4.4 Reduce the 9% repayment rate on graduate earnings above the repayment threshold, as this limits the disposable income of young workers who are already under an enormous amount of financial pressure from high housing costs and stagnant wages. IF's 2019 research found that the average 20-something has to spend 67% of weekly expenditure on essentials, leaving little left over to save for life's milestones such as moving out of the family house, renting, or buying a home of their own.[5]

4.5 Bring student loans under the auspices of the Consumer Credit Act 1974, which would protect borrowers from the terms under which they originally took out their student loans being revised in ways that were unfavourable to them. This is necessary because the government has already reneged on the original terms of student loans once when it chose to freeze the student loan repayment threshold in 2015 rather than allowing it to rise in line with inflation, which made repayments more expensive for borrowers.

5. End the Triple Lock

(and maybe increase pensioner credit to protect poorer pensioners)

5.1 IF continues to endorse the ending of the triple lock on Pensions. In 2017 pensioners' average household income overtook that of the average working family. Further, since the introduction of the triple lock in 2007, pensioner poverty has fallen year on year to just 16%, almost half that of children. While remaining pensioner poverty is still a serious issue, the triple lock has served its purpose in bringing pensioners back into line. IF suggests downgrading to a double lock, where pensions are linked to the higher of earnings and inflation, which would keep pensions rising with living costs but not unfairly privileging them during times of economic hardship.

6. Eliminate VAT on costs of in-situ subdivision of homes

6.1 IF research suggests that there are up to 4.4 million homes that have the potential for "downsizing-in-situ" (where older people subdivide their homes.[6] It would free up a significant amount of accommodation within cities, diversify ageing neighbourhoods and allow older people to remain in their communities at a time in their lives that familiarity and stability are highly valued. A VAT exemption could encourage older under-occupying households to downsize within their own homes, as well as provide an additional income boost through either renting or selling the new unit created.

For further information please contact:

Liz Emerson on mobile: 07971 228823

Email: liz@if.org.uk

[5] Kingman, D. (2019) All Consuming Pressures: The cost-of-living crisis facing younger generations http://www.if.org.uk/research-posts/all-consuming-pressures-the-cost-of-living-crisis-facing-younger-generations/

[6] Kingman, D. (2015) Unlocking England's Hidden Homes: http://www.if.org.uk/research-posts/unlocking-englands-hidden-homes/