



House of Commons
Treasury Committee

Budget 2014

Thirteenth Report of Session 2013–14



House of Commons
Treasury Committee

Budget 2014

Thirteenth Report of Session 2013–14

*Report, together with formal minutes relating
to the report*

*Ordered by the House of Commons
to be printed 7 May 2014*

The Treasury Committee

The Treasury Committee is appointed by the House of Commons to examine the expenditure, administration, and policy of HM Treasury, HM Revenue and Customs and associated public bodies.

All publications of the Committee (including press notices) and further details can be found on the Committee's web pages at www.parliament.uk/treascom.

Membership at time of the report

[Mr Andrew Tyrie MP](#) (*Conservative, Chichester*) (Chairman)
[Mark Garnier MP](#) (*Conservative, Wyre Forest*)
[Stewart Hosie MP](#) (*Scottish National Party, Dundee East*)
[Andrea Leadsom MP](#) (*Conservative, South Northamptonshire*)
[Mr Andy Love MP](#) (*Labour, Edmonton*)
[John Mann MP](#) (*Labour, Bassetlaw*)
[Mr Pat McFadden MP](#) (*Labour, Wolverhampton South West*)
[Mr George Mudie MP](#) (*Labour, Leeds East*)
[Mr Brooks Newmark MP](#) (*Conservative, Braintree*)
[Jesse Norman MP](#) (*Conservative, Hereford and South Herefordshire*)
[Teresa Pearce MP](#) (*Labour, Erith and Thamesmead*)
[David Ruffley MP](#) (*Conservative, Bury St Edmunds*)
[John Thurso MP](#) (*Liberal Democrat, Caithness, Sutherland, and Easter Ross*)

Powers

The Committee is one of the departmental select committees, the powers of which are set out in House of Commons Standing Orders, principally in SO No 152. These are available on the Internet via www.parliament.uk.

Publication

The Reports and evidence of the Committee are published by The Stationery Office by Order of the House. All publications of the Committee (including press notices) are on the Internet at www.parliament.uk/treascom.

The Reports of the Committee, the formal minutes relating to that report, oral evidence taken and some or all written evidence are available in printed volume(s). Additional written evidence may be published on the internet only.

Committee staff

The current staff of the Committee are Chris Stanton (Clerk), Anne-Marie Griffiths (Second Clerk), Adam Wales (Senior Economist), Hansen Lu, Thomas Francis (on secondment from the FCA), Gregory Stevens (on secondment from the Bank of England), and Callum Saunders (on secondment from the NAO) (Committee Specialists), Steven Price (Senior Committee Assistant), and Alithea Williams and Paul Little (Committee Assistants).

Contacts

All correspondence should be addressed to the Clerk of the Treasury Committee, House of Commons, 7 Millbank, London SW1P 3JA. The telephone number for general enquiries is 020 7219 5769; the Committee's email address is treascom@parliament.uk

Contents

Report	<i>Page</i>
1 Introduction	4
Our inquiry	4
Compliance with principles of tax policy	5
The Office for Budget Responsibility	5
Leaks and advance briefing	6
2 Macroeconomy	8
Prospects for growth	8
Business investment	10
Trade and global headwinds	12
Spending, saving and debt	14
The housing market	18
Productivity and the output gap	22
3 The public finances	25
Performance against the fiscal targets	25
Changes announced in the Budget	26
Cyclically adjusted current budget	29
Ring fencing	31
Welfare cap	33
4 Pension reforms and savings	39
Increasing pension flexibility	39
Past reforms	39
Immediate changes	39
Pension reforms from April 2015	41
The importance of choice	42
The responsibility of choice	43
Auto-enrolment	43
The uncertain impact of the reforms	44
Falling back on to the welfare state	45
Longevity risk	49
Financial innovation	50
The guidance guarantee	56
Guidance, advice and consumer protection	58
When should guidance be made available?	59
Developing the guidance guarantee and the Money Advice Service	60
Who should deliver the guidance guarantee?	60
Who will pay for the guidance guarantee?	61
Interaction with existing and proposed Government sponsored guidance	62
Principles for the 'guidance guarantee'	65
Impact on the wider economy	65
Defined benefit schemes	65

Changes in consumption and asset allocation	67
Future infrastructure investment	68
Relationship to other savings reforms	69
Pensioner bonds	72
5 Taxation	76
Principles of taxation	76
Retrospection and anti-avoidance	77
HMRC debt recovery powers	79
Savings rate of income tax	86
Annual Investment Allowance	88
6 Parliamentary timing	90
Conclusions and recommendations	92
Principles of Tax Policy and Budget 2014	99
Introduction	99
Basic fairness	99
Supporting growth and encouraging competition	100
Certainty, including simplicity	101
Stability	102
Practicality	103
Coherence	104
Conclusion	105
The Chartered Institute of Taxation	105
The Association of Taxation Technicians	105
The Low Incomes Tax Reform Group	106
Traffic light assessment	107
About ICAEW	107
About ICAEW	108
Detailed comments	108
Pensions reform	108
Personal allowance increased by £500 to £10,500	108
Annual investment allowance (AIA) doubled to £500,000, until end of 2015	108
Anti-avoidance: £4bn revenue forecast, increased funding for HMRC non-compliance team	109
HMRC power to access debtor accounts	109
15% stamp duty land tax on £500,000 residential properties in corporate entities	109
Seed Enterprise Investment Scheme made permanent	110
Increased limits for ISAs, abolition of distinctions between cash and share-based savings	110
Abolishing 10% starting rate for savings income	110
About ACCA	112
Comments on the Budget	112
Appendix 1: Chartered Institute of Taxation	99

Appendix 2: Institute of Chartered Accountants in England and Wales	107
Appendix 3: Association of Certified Chartered Accountants	112
Formal Minutes	117
Witnesses	118
List of additional written evidence	119
List of Reports from the Committee during the current Parliament	120

1 Introduction

Our inquiry

1. The Committee took evidence from nine panels of witnesses during the five meetings we held, as follows:

25 March: City economists and the Institute for Fiscal Studies

First panel: Paul Mortimer-Lee, Global Head of Market Economics, BNP Paribas; Michael Saunders, Head of West European Economics, Citi; Rob Wood, Chief UK Economist, Berenberg Bank.

Second panel: Paul Johnson, Director and Gemma Tetlow, Programme Director, Institute for Fiscal Studies.

27 March: Office for Budget Responsibility

Robert Chote, Chairman, Graham Parker CBE, Member, and Professor Stephen Nickell CBE, Member, Budget Responsibility Committee.

1 April: Financial Conduct Authority; consumer and industry representatives

First panel: David Geale, Head of Savings, Investments and Distribution and Chris Woolard, Director of Policy, Risk and Research, Financial Conduct Authority.

Second panel: Dr Ros Altmann, pensions policy, investment banking, savings and retirement expert, and Jane Vass, Head of Public Policy, AgeUK.

Third panel: Chris Hannant, Director General, Association of Professional Financial Advisors, Robin Fieth, Chief Executive, Building Societies Association, and Joanne Segars, Chief Executive, National Association of Pension Funds.

3 April: HM Treasury

Rt Hon George Osborne MP, Chancellor of the Exchequer, Sir Nicholas Macpherson KCB, Permanent Secretary, and James Bowler, Director, Strategy, Planning and Budget.

8 April: Association of British Insurers; professional accounting and tax bodies

First panel: Otto Thoresen, Director General, Association of British Insurers.

Second panel: Andrew Courts, Member, ACCA Global Tax Forum, Frank Haskew, Head of Tax Faculty, Institute of Chartered Accountants in England and Wales, and Patrick Stevens, Tax Policy Director, Chartered Institute of Taxation.

2. We are very grateful to all our witnesses and to those who submitted written evidence. Their willingness to provide evidence within the short timescale available for this inquiry is particularly appreciated.

Compliance with principles of tax policy

3. We have continued our innovative practice, begun in 2011, of asking three professional accounting and tax bodies—the Association of Certified Chartered Accountants, the Institute of Chartered Accountants of England and Wales, and the Chartered Institute of Taxation—to provide the Committee with written evidence on the extent to which the provisions of the Budget, and the Finance Bill which will implement them, meet the criteria set out in our Report of 2011, *Principles of Tax Policy*.¹ The principles are: fairness; supporting growth and encouraging competition; certainty, including simplicity; stability; practicality; and coherence.

4. This year, in view of the importance of this work, we asked the three professional bodies to give oral evidence to us, in addition to their written submissions. We are very grateful to these bodies for their assistance in our work. We have drawn extensively on their evidence in Chapter 5 of this Report, in which we consider in detail the extent to which this year's Budget measures comply with our principles.

The Office for Budget Responsibility

5. The Office for Budget Responsibility (OBR) states in the *Economic and Fiscal Outlook* that accompanied the Budget that “we have come under no pressure from Ministers, advisers or officials to change any of our conclusions” and that “we have been provided with all the information and analysis that we requested”.² The Chairman of the OBR repeated these assurances to us in oral evidence.³

6. The OBR was not, however, informed of the Government's plans to extend childcare support to all families eligible for Universal Credit until after the deadline for the submission of new policies to the OBR had passed. In a briefing following the Budget, the Chairman of the OBR, Robert Chote, said:

Regrettably, our forecasts do not include the costs of the Government's announcement yesterday that it will extend childcare support to all families on Universal Credit, and not just those paying income tax. We were only notified of this announcement on Monday evening, well after the EFO had been sent to the printers and almost a week after the deadline for us to be notified of new policies.

The Government claims that the cost of this measure will be around £200 million a year. It would have been much better for this costing to have been subjected to proper scrutiny and to be included in our forecasts, along with every other policy measure that affects the public finances. To say that the cost to the Exchequer will be

1 Eighth Report of Session 2010–11, *Principles of Tax Policy*, [HC 753](#)

2 Office for Budget Responsibility, *Economic and Fiscal Outlook*, [Cm 8820](#), March 2014, Foreword, p 3

3 Q98

offset later by some as-yet-unidentified changes to Universal Credit is no excuse. We will look at this measure, and any accompanying measures, very closely in the run-up to the Autumn Statement.⁴

7. It is regrettable that the Government did not supply details of its additional support for childcare to the OBR in time for it to verify the Government’s claims about the costs of this policy. The OBR has said that it will look at this measure closely in the run up to the Autumn Statement. It is not acceptable, however, that the Government’s figures should be left unverified for what may be more than eight months. We recommend that, when Budget announcements are not submitted before the OBR’s deadline, the OBR should scrutinise major uncosted policies as soon as reasonably possible thereafter and publish its findings.

Leaks and advance briefing

8. This Committee deprecates both leaks and advance briefing of Budget announcements. In 2013, following the premature release of Budget information by the *Evening Standard*, we recommended that “there should be no Treasury pre-releasing of Budget information, even in secure conditions.”⁵ The Chancellor asked Sir Nicholas Macpherson, Permanent Secretary to the Treasury, to undertake a review of the practice of pre-releasing of Budget information under embargo on Budget day. Sir Nicholas recommended that the Treasury introduce “a ban on the pre-release of the core of the Budget (and Autumn Statement), that is: the economic and fiscal projections, the fiscal judgement and individual tax rates, reliefs and allowances.”⁶

9. This year, we were pleased to note that the key Budget measures did not appear in the press in advance of the Chancellor’s statement to the House of Commons. In particular, the pension reforms announced in the Budget were not leaked or pre-briefed. Otto Thoresen, Director General, Association of British Insurers, told us that the Budget announcements had come as “a genuine surprise to everybody”.⁷ We asked Sir Nicholas Macpherson, Permanent Secretary to the Treasury, how this level of secrecy had been achieved. He told us:

There was an agreement last year about the way we were going to approach the Budget, especially about not pre-briefing the main elements of it, and everybody was extraordinarily well disciplined, which was really important in the context of the pension proposals that, as you know, were very market sensitive.⁸

10. We welcome the fact that the Government maintained the confidentiality of the Budget this year. This can only have helped the presentation of the Budget measures. This Budget was unusual, however, in that one of its most important components—the reform of pensions—was highly market sensitive: the rules against selectively disclosing

4 Office for Budget Responsibility, [Economic and Fiscal Outlook Briefing](#), 19 March 2014

5 Ninth Report of Session 2012–13, *Budget 2013*, [HC 1063](#), para 205

6 HM Treasury, [Review into the pre-release of Budget information](#), July 2013, para 5.3

7 Q454

8 Q363

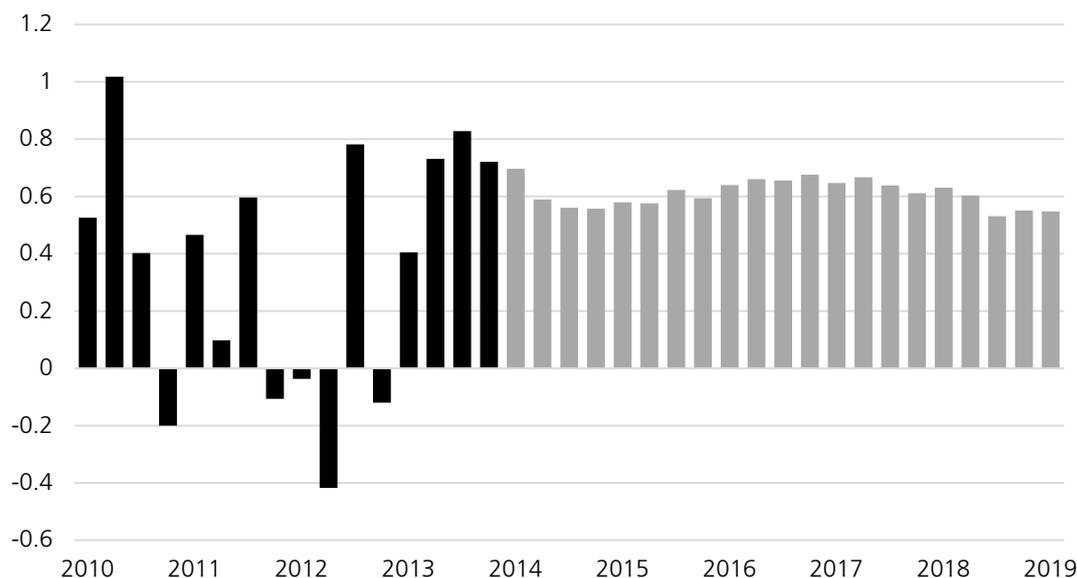
market sensitive information appear to have constituted a powerful enough deterrent to advance briefing of those reforms. We will expect this year's good practice in maintaining confidentiality to be maintained in future Budgets, when such considerations do not necessarily apply.

2 Macroeconomy

Prospects for growth

11. Figures from the Office for National Statistics (ONS) show that the UK's economic recovery maintained momentum through to the end of 2013. Compared with the previous year, Gross Domestic Product (GDP) is estimated to have grown by 1.7 per cent,⁹ 0.3 percentage points (pp) higher than the Office for Budget Responsibility (OBR) had forecast in December 2013.¹⁰

Chart 1: OBR's real GDP growth forecasts (per cent)



Note: Per cent, quarter-on-quarter; ONS estimates Q1-2010 to Q4-2014 (black) and OBR forecasts Q1-2014 to Q1-2019 (grey)

Sources: ONS, Quarterly National Accounts, Q4 2014, dataset series ABMI; Office for Budget Responsibility, Economic and Fiscal Outlook – March 2014, supplementary economy table 1.1

12. In its March 2014 Economic and Fiscal Outlook, the OBR revised up its forecasts for GDP growth in 2014 and 2015 by 0.3pp and 0.1pp respectively.¹¹ These changes were driven primarily by upward revisions to its forecasts for business investment. But the OBR lowered its forecast for growth in 2018 by 0.3pp. It explained this revision as follows:

The combination of a slightly stronger near-term outlook for GDP growth and a slightly narrower output gap forecast in December means the output gap is now expected to close by mid-2018, around a year earlier than in our December forecast. Since we assume that growth will be in line with its trend rate once the output gap

9 ONS, Quarterly National Accounts, Q4 2014, dataset series [IHYP](#)

10 OBR, [Economic and Fiscal Outlook – December 2013](#), Table 1.1

11 OBR, [Economic and Fiscal Outlook – March 2014](#), Table 1.1

has closed, rather than forecasting further cyclical fluctuations around that trend, we have revised our GDP growth forecast in 2018 down slightly.¹²

Table 1: OBR's real GDP growth forecasts (percent)

	December 2013 Economic and Fiscal Outlook	March 2014 Economic and Fiscal Outlook	Change (percentage points)*
2013	1.4	1.8	0.3
2014	2.4	2.7	0.3
2015	2.2	2.3	0.1
2016	2.6	2.6	0.0
2017	2.7	2.6	0.0
2018	2.7	2.5	-0.3

* change may not equal difference between December 2013 and March 2014 columns due to rounding

Source: Office for Budget Responsibility, *Economic and Fiscal Outlook (December 2013 and March 2014 editions)*, Table 1.1

13. The OBR's projections for growth in the short term sit just below the median of those made by major independent forecasters in March 2014. Forecasts for growth in 2014 range from 2.5 per cent to 3.3 per cent. For 2015, forecasts range from 2.0 per cent to 3.2 per cent.¹³ In its *World Economic Outlook*, published on 10 April 2014, the IMF forecast growth in the UK of 2.9 per cent in 2014 and 2.5 per cent in 2015.¹⁴

14. The pick-up in growth through 2013 took many economists by surprise. In explaining the origins of the recovery, the OBR acknowledged that “the ongoing weakness of productivity, real incomes and UK export markets over this period make it difficult to explain why activity has picked up as strongly as it has.”¹⁵ However, in evidence to the Committee, Robert Chote, Chairman of the OBR, said that “a combination of factors” explained why the recovery took hold when it did, including:

[...] a general improvement in confidence; the fact that the external environment is seen to be less threatening; looking directly at it, you would infer that there is slightly less of a drag from fiscal consolidation over this period than in the earlier period as well, so that would have an impact. On the business investment side, in addition to demand issues, you also have a greater need for replacement of investment, and the longer investment is weak the more powerful that becomes as a factor.¹⁶

15. Other economists agreed that heightened consumer and business confidence, a more benign global economic environment, and some reduction in the pace of fiscal

12 OBR, [Economic and Fiscal Outlook – March 2014](#), p.9

13 HM Treasury, [Forecasts for the UK economy: a comparison of independent forecasts, March 2014](#), Table 4 and Table 7

14 IMF, [World Economic Outlook database April 2014](#)

15 OBR, [Economic and Fiscal Outlook – March 2014](#), p.54

16 Q112

consolidation have all played a role in the recovery. Measured by the change in real-terms public sector net borrowing, there was a fiscal consolidation of £39.2bn between 2011–12 and 2012–13, but a forecast fiscal loosening of £13.3bn between 2012–13 and 2013–14.¹⁷ Paul Mortimer-Lee, head of market economics at BNP Paribas, said:

What we saw was a removal of headwinds [...] the crisis in Europe abated and that allowed optimism to come forward. There were measures to stimulate the housing market. We have to say that the pace of structural fiscal tightening was rather less than it had been in previous years.¹⁸

Michael Saunders, Head of West European Economics at Citi said that “the shift from very heavy fiscal restraint to almost no fiscal restraint in 2012, 2013 and 2014” had “lifted a headwind”.¹⁹

16. The OBR identified a number of risks to the recovery, which are examined in more detail in the rest of this chapter. When asked about the sustainability of the recovery, Mr Chote said:

I think productivity, earnings and the consumption story have to come right. In business investment, the recent tentative signs of improvement need to be sustained.²⁰

Business investment

17. The OBR expects a strong revival in business investment, with real terms growth averaging 8.3 per cent per year during 2014–18.²¹ Over this forecast period, business investment is expected to account for a quarter of growth—even though it currently represents just 8 per cent of GDP.²²

18. The forecast is grounded in the strong pick-up in investment activity during the second half of 2013, together with business survey data which indicated both reduced uncertainty about future demand, and stronger investment intentions.²³ The strength of corporate finances, and the fact that business investment is more than 20 per cent below its pre-crisis peak, are, according to the IFS Green Budget, further reasons to believe that there is significant scope for growth.²⁴

19. By the end of the forecast period, the OBR expects business investment to reach 10.9 per cent GDP, a level only achieved briefly on one occasion in the past 40 years.²⁵ When

17 OBR, [Public finances databank](#), 26 Mar 2014

18 Q9

19 Q25

20 Q114

21 OBR, [Economic and Fiscal Outlook – March 2014](#), Table 1.1

22 ONS, Quarterly National Accounts, Q4 2014, dataset series [NPEL](#) and [ABMI](#)

23 OBR, [Economic and Fiscal Outlook – March 2014](#), p.70

24 Institute for Fiscal Studies, [Green Budget](#), February 2014, p.70

25 OBR, [Economic and Fiscal Outlook – March 2014](#), [charts and tables data](#), Chart 3.37

asked whether this was plausible, Mr Chote noted that a business investment to GDP ratio of 10.9 per cent was unexceptional by international standards:

[...] what is quite striking is that investment, in aggregate, tends to be relatively low in the UK compared to other countries and there may be a variety of long-term structural issues that help to address that. For example, planning could be restricting investment across a wide range of areas, but the sorts of increases in investment ratios as a share of GDP that we have in this forecast would still leave us with a rate that looks relatively modest compared to the OECD average over the past 10 years or so.²⁶

20. Despite its positive forecast for business investment, the OBR noted that “it remains to be seen whether the recent pick-up in business investment indicates a turning point in investment spending”.²⁷ Mr Chote added that the OBR had “predicted pick-ups in business investment before that have not materialised”, adding that “the data is hard to interpret. There is tentative evidence.”²⁸

21. Other economists expressed differing views about the likelihood and strength of the recovery in business investment. Mr Saunders wrote that “we are reasonably confident about the prospects for such an investment pick-up”²⁹ and in oral evidence pointed to the fact that “corporate balance sheets and aggregates are in terrific shape with very strong liquidity” as grounds for such optimism.³⁰ Mr Mortimer-Lee thought that investment would grow strongly in the short term thanks to the ‘catch up’ necessitated by postponed investment plans, but questioned how long this could be sustained:

The problem I have with the OBR’s forecast is that this pick-up in investment goods demand seems to last for ever at almost double digit rates, and it is scarcely ever like that. There tend to be surges and spirits change, people catch up. You get a peak and then it comes off again, and I think that is much more likely than the OBR’s forecast.³¹

22. Even as confidence and optimism recover, there may remain structural factors that continue to inhibit business investment. Although the funding picture for larger firms has improved, access to finance may remain a problem for SMEs which want to invest. Robert Wood, Chief UK Economist at Berenberg Bank, said that “very poor availability of finance over the past few years has almost certainly prevented some rapidly growing firms from expanding”.³² The CBI wrote that “SME underinvestment is a structural rather than a cyclical problem” and recommended broadening the range of financing sources available to smaller firms as a means of tackling this.³³ Among larger companies, the Kay Review of

26 Q124

27 OBR, [Economic and Fiscal Outlook – March 2014](#), p.71

28 Q114

29 Citi Research, Budget reinforces strong growth/low inflation outlook, 19 March 2014, p.3

30 Q15

31 Q30

32 Q23

33 CBI, written evidence

equity markets has described how short-termism among shareholders can manifest itself in under-investment.³⁴

23. Investment is important for the recovery in the short term, but it is also needed to drive the productivity growth necessary for sustainable growth in the longer term. As Ian McCafferty, external member of the Monetary Policy Committee, put it in a recent speech:

Business investment is a crucial element to the recovery. It does not just contribute to cyclical fluctuations in the economy; as the means by which the stock of capital accumulates, it also influences the productive capacity of the economy and long-term trends in growth.³⁵

Trade and global headwinds

24. The OBR and the Chancellor both agreed that the UK's export performance since the financial crisis had been disappointing.³⁶ Their assessment chimes with that of the IFS Green Budget, which described export growth since 2008 as “disappointing, especially when considering the sharp depreciation of sterling during 2008–09”,³⁷ and the IMF, which described the UK's recovery to date as “unbalanced, with business investment and exports still disappointing”.³⁸

25. In explaining the UK's export performance, economists we heard from agreed with the OBR that weak global demand, particularly in the Eurozone and US, which together account for 55 per cent of UK exports,³⁹ had played a significant role. However, the IFS Green Budget suggested that “structural failings within the domestic economy” were also to blame.⁴⁰ It went on to cite a recent report from the Ernst and Young ITEM Club, which found:

Evidence that exporters' efficiency has been hampered by factors such as red tape, the poor access SMEs to trade finance and a prolonged period of underinvestment in the transport and communications infrastructure networks. These problems have slowed the UK's pace of expansion into fast-growing emerging markets and limited the ability of exporters to capitalise on an increase in external demand.⁴¹

The Chancellor also believed that a failure to gain a foothold in emerging markets had held back UK exports:

I think that the UK found itself in a situation where it was overly dependent on mature markets, the European Union, the European markets, the United States. We

34 [The Kay Review of Equity Markets and Long-term Decision Making](#), July 2012, p.10

35 Ian McCafferty, [Achieving a sustainable recovery: where next for business investment?](#) Speech to Nottingham Business School, 22 January 2014, p.2

36 OBR, [Economic and Fiscal Outlook – March 2014](#), p.71; Q375

37 Institute for Fiscal Studies, [Green Budget](#), February 2014, p.70

38 IMF, [World Economic Outlook, April 2014](#), p.53

39 ONS, United Kingdom Economic Accounts, Q4 2013, dataset series [K9HQ](#) and [LGIW](#)

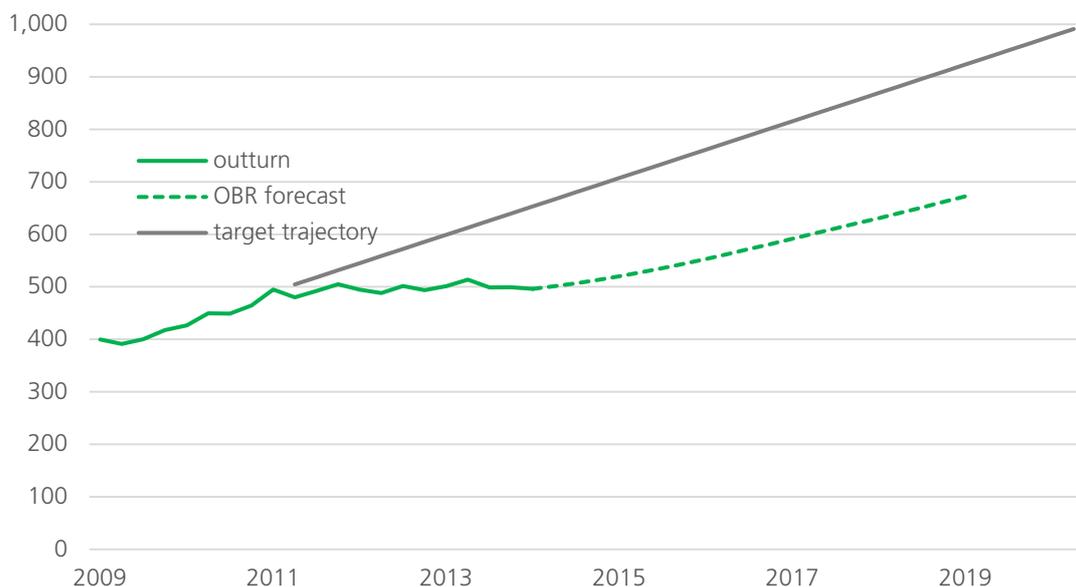
40 Institute for Fiscal Studies, [Green Budget](#), February 2014, p.71

41 Institute for Fiscal Studies, [Green Budget](#), February 2014, p.71

were not connected into China, India, Brazil and the new growing markets of the world.⁴²

26. By the first quarter of 2019, the OBR expects exports to reach £672 billion on an annualised basis, well short of the Chancellor’s target of £1 trillion by 2020.⁴³ Imports are expected to grow at a similar rate, leaving net trade (exports minus imports) making no contribution to growth over the coming five years.⁴⁴ The IFS Green Budget forecast “modest positive contributions” to growth from net trade, with export growth underpinned by a shift towards emerging markets.⁴⁵ By contrast, Mr Mortimer-Lee believed the OBR’s assessment to be unduly optimistic. He told us that ongoing weakness in the Eurozone meant the export growth implied by their forecasts was “too rapid”.⁴⁶

Chart 2: UK exports and target trajectory to reach £1 trillion by 2020



Sources: ONS Balance of Payments Q4 2013, dataset series [IKBH](#); OBR, *Economic and Fiscal Outlook – March 2014*, [supplementary economy tables](#), Table 1.2; HM Treasury, *Budget 2012*, p.43

27. The OBR, however, identified to a number of global risks that could affect the outlook for trade and the wider economy. These include the effects of capital flight on emerging markets of a tightening of monetary policy in advanced economies, particularly the US; the failure of “euro area economies and banking systems [...] to complete the adjustment toward sustainable demand and competitiveness”, particularly in an environment of very low inflation; and an escalation of political instability in Ukraine.⁴⁷

42 Q375

43 OBR, *Economic and Fiscal Outlook – March 2014*, [supplementary economy tables](#), Table 1.2; HM Treasury, [Budget 2012](#), p.43

44 OBR, [Economic and Fiscal Outlook – March 2014](#), p.57

45 Institute for Fiscal Studies, [Green Budget](#), February 2014, p.71

46 BNP Paribas, [written evidence](#)

47 OBR, [Economic and Fiscal Outlook – March 2014](#), p.81-82

Spending, saving and debt

28. The OBR wrote that “consumer spending, supported by a falling saving ratio, has been the biggest driver of recent growth”.⁴⁸ In the face of weak real income growth, this spending has been financed by a reduction in savings: between 2012 and 2013, the savings ratio fell by 2.2pp from 7.3 per cent to 5.1 per cent, its sharpest year-on-year fall since at least 1988.⁴⁹

29. The IFS Green Budget summarised the factors it believed provided the impetus for this shift from saving to spending during 2013:

This switch to a lower rate of saving reflected a strengthening in consumer confidence over the course of the year, which was underpinned by falling unemployment and which induced consumers to lower levels of precautionary saving. It was also a function of a steady decline in deposit rates, acting to reduce incentives to save and encouraging people to spend more.⁵⁰

Mr Wood added that an easing of credit conditions had buoyed consumer sentiment and encouraged a reduction in saving:

I think what has been key for the recovery is an easing in credit conditions, the fact that people know they can borrow if they need to, the fact that the conditions on their mortgages have eased so they know if they need to remortgage they can, and I think that has allowed them to cut back their saving.⁵¹

30. The OBR, and other economists from whom we heard, agreed, however, that rising consumption could not be financed by falling savings indefinitely, and that spending growth would soon have to fall back into line with real income growth. Mr Chote said:

[...] the reason that we have some slowing [in output growth] is that consumer spending was driven in part by the fact that you have the saving ratio falling from 7.2 per cent to 5 per cent during 2013, contributing to greater consumer spending, and that we would not expect the saving ratio to continue to fall at that sort of rate. What we have is consumer spending moving more into line with underlying income growth, and underlying income growth, in time, will be boosted by improvements in productivity growth, we hope.⁵²

The IFS Green Budget also forecast that the path of consumer spending would soon begin to follow that of real incomes: “As the household savings ratio levels out, consumer spending is expected to realign and more closely follow the evolution of income growth over the next two years.”⁵³

48 OBR, [Economic and Fiscal Outlook – March 2014](#), p.5

49 ONS, Quarterly National Accounts, Q4 2014, dataset series [NRJS](#)

50 Institute for Fiscal Studies, [Green Budget](#), February 2014, p.64

51 Q21

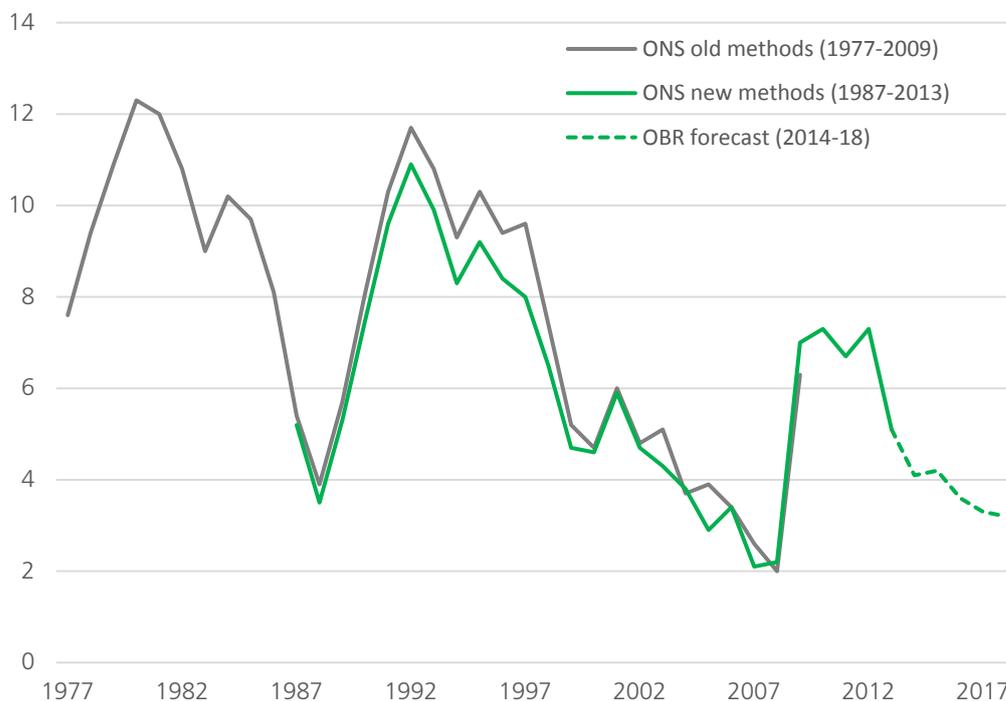
52 Q113

53 Institute for Fiscal Studies, [Green Budget](#), February 2014, p.65

31. Even with real household incomes growing throughout the forecast period, the OBR expects that consumption will continue to be financed in part by falling savings. The savings ratio is expected to carry on falling, albeit at a slower rate, throughout the forecast period. By 2018, it is forecast to reach 3.2 per cent,⁵⁴ well below its average of 6.1 per cent over the period 1987–2013.⁵⁵ When asked whether this was a cause for concern, the Chancellor said:

To put this in context [...] on the eve of the financial crisis, it was 0.2 per cent, so it has been much lower in our recent history. What I do want to do is incentivise saving and that was a central part of what the Budget was all about.⁵⁶

Chart 3: Savings ratio



Note: Percentage of disposable income saved; annual; ONS figures 1977-2013 (under two different methods) and OBR forecasts 2014-18

Sources: ONS, Quarterly National Accounts, Q4 2014, dataset series [NRJS](#); OBR, [Economic and Fiscal Outlook – March 2014](#), p.87

32. Professor Steve Nickell of the Budget Responsibility Committee avoided expressing a view on whether there was a desirable level for the savings ratio, but noted that “before the crash, it had probably got to a level that was too low”, adding that “what one does not wish to see is long trends, particularly downwards, in the savings rate”.⁵⁷

54 OBR, [Economic and Fiscal Outlook – March 2014](#), p.87

55 ONS, Quarterly National Accounts, Q4 2014, dataset series [NRJS](#)

56 Q378

57 QQ137-8

33. In his speech to the House, the Chancellor indicated that the reforms to pensions proposed in the Budget would address low levels of saving and high levels of borrowing:

Our tax changes will help people in work, but there is a large group who have had a particularly hard time in recent years, and that is savers. This matters not just because they are people who have made sacrifices to provide for their own economic security in retirement. It matters too because one of the biggest weaknesses of the British economy is that it borrows too much and saves too little [...] so today we put in place policies for savers that stand alongside deficit reduction as a centrepiece of our long-term economic plan.⁵⁸

34. In its forecast, the OBR acknowledged that there was considerable uncertainty about the effects of the pensions and savings measures on saving and spending, but on balance assessed their effect to be neutral:

As we consider the principal effect of these [pensions and savings] measures will be on the composition of household assets, rather than aggregate flow of saving or spending, we have not adjusted our forecast for these measures.⁵⁹

Mr Chote reiterated this in evidence to the Committee, saying:

We are assuming that, if you look at the set of pension and saving measures in total, there are effects going in both directions and, therefore, we have not made an explicit adjustment to the forecast for that. That is not because we are very confident that the answer is zero. It is because there are things going in both directions and we do not think we can be clear which way wins out [...] it does not seem to us that there is powerful enough evidence to say we can be very confident the effect is either net positive or negative net.⁶⁰

35. The economists we heard from differed in their view as to the effect of the measures, but agreed that there was significant uncertainty. Mr Wood said “frankly, I don’t know how big the number would be but I think directionally it would be positive for consumption”.⁶¹ Mr Mortimer-Lee said “I agree that there will be a short-term boost to demand and to tax revenues. Longer term, people may actually save more”.⁶²

36. When asked about the OBR’s view that the pensions and savings measures would not affect the savings ratio, the Chancellor suggested that their assessment was coloured by the fact that the measures had not yet been put into law:

I think the OBR are right to take the cautious approach. That is because they are the cautious, independent forecasting body and they want to see the proof in the

58 [HC Deb, 19 March 2014, c792](#)

59 OBR, [Economic and Fiscal Outlook – March 2014](#), p.42

60 Q204

61 Q48

62 Q51

pudding. They want to see that what I announce on Budget day becomes the law of the land and is implemented.⁶³

37. The OBR also forecasts a rising household debt-to-income ratio, from 141.9 per cent at the end of 2013 to 165.7 per cent by the beginning of 2019, close to its pre-crisis peak of 169.9 per cent.⁶⁴ Mr Chote said that this growth was driven predominantly by the housing market and “a pick-up in house prices and a pick-up in the size and the number of mortgages”.⁶⁵ He drew a distinction between the falling savings ratio, which had driven the recent growth in spending, and rising household debt, which was a “balance sheet story [...] You can have an increase in the household debt-to-income ratio that is not a particularly important part of the consumption story. It is just because houses are more expensive”.⁶⁶

38. The economists we heard from were divided about whether the rising debt-to-income ratio forecast by the OBR was worrying. Mr Saunders questioned the forecast itself, saying:

[...] the OBR have been forecasting [a rising debt-to-income ratio...] for a while and in practice it has tended to undershoot their forecasts. Even now the debt-to-income ratio is still falling [...] We may yet come to a point a few years down the road at which household debt has risen sharply and we are back to the credit excesses of 2006–07, but I don’t think that is where we are now.⁶⁷

Mr Wood believed that rising debt could increase vulnerability in the event of a downturn:

Turning back to sustainability, I don’t think [...] the recovery is going to end in the next two or three years because households are releveraging, but I think when we do get another downturn it does make us much more vulnerable.⁶⁸

Mr Mortimer-Lee was more concerned. He said:

I am quite worried about the picture the OBR paints of debt going back to 2 per cent below the peak levels because people are making decisions on debt currently on the basis of interest rates that are extraordinarily low [...] there will be an adverse shock to household income gearing, to household cash flow, as the debt built up at low interest rates has to be serviced at much higher interest rates. That is a real recession risk towards the end of this forecast period, I think.⁶⁹

39. The sensitivity of household finances to changes in monetary policy was examined by the OBR. Its central forecast assumes that the Bank of England rate rises in line with market expectations to reach 3 per cent by the start of 2019, but that mortgage rates rise only 0.8 percentage points in response. In this scenario, it estimates that 5.5 per cent of

63 Q383

64 OBR, Economic and Fiscal Outlook – March 2014, [charts and tables data](#), Chart 3.33

65 Q133

66 Q135

67 Q17

68 Q22

69 Q18

households would have to adjust their behaviour by spending less, working longer hours, or changing their mortgage terms.⁷⁰ However, the results are substantially altered if it is assumed that changes in the Bank rate feed through one-for-one to mortgage interest rates:

If mortgage rates were to rise by 2.5 percentage points by Q1 2019, in line with our central assumption for the Bank rate, the effect on borrowers could be more significant, with 24 per cent of mortgagors changing behaviour.⁷¹

The housing market

40. Housing market activity has continued to pick up, supported by Government policy, low interest rates and greater mortgage availability. The OBR summarised recent developments thus:

Residential property transactions accelerated again in the final quarter of 2013, rising by 8 per cent from the previous quarter and 26 per cent on a year earlier. Mortgage approvals have also accelerated, suggesting further growth in transactions in the near term. Both are being boosted by a substantial fall in mortgage interest rates and improved confidence, and by the Government's Help to Buy scheme.⁷²

41. This activity has been reflected in rising house prices. According to the Nationwide index, prices grew by 9.2 per cent across the UK in the 12 months to March 2014. In London, prices increased by 18.2 per cent over the same period, their fastest rate of growth since 2003.⁷³ The Land Registry and Halifax house price indices show similar trends. Adjusting for consumer price inflation, however, house prices remain 22 per cent below their peak across the UK and 6 per cent below peak in London.⁷⁴ Market activity, measured by mortgage lending or housing transactions, is also below its pre-crisis peak.⁷⁵

42. Nonetheless, concerns have been expressed that the housing market is entering a bubble, defined by Professor Nickell as “when demand is being driven by people wanting to get in because of expectation of price growth rather than as somewhere to live”⁷⁶ and in the IFS Green Budget as when “asset prices are driven by expectations of future price increases rather than by the intrinsic value of the asset involved.”⁷⁷ If this were the case, house prices would be more vulnerable to a sharp decline in the future.

43. Mr Chote believed that recent developments in the housing market could be adequately explained without reference to such speculative behaviour:

I think you are basically seeing a pick-up in demand for housing, partly as a result of confidence and partly the ability for people to get hold of mortgages, but you have a

70 OBR, [Economic and Fiscal Outlook – March 2014](#), p.69-70

71 OBR, [Economic and Fiscal Outlook – March 2014](#), p.70

72 OBR, [Economic and Fiscal Outlook – March 2014](#), p.67

73 [Nationwide house price index data](#) – regional and quarterly series

74 [Nationwide house price index data](#) and ONS consumer prices dataset, February 2014, series [D7BT](#)

75 Institute for Fiscal Studies, [Green Budget](#), February 2014, p.91

76 Q145

77 Institute for Fiscal Studies, [Green Budget](#), February 2014, p.101

very unresponsive supply of housing. Therefore, you can explain an increase in house prices by fundamentals without having to resort to saying that there is a bubble going on.⁷⁸

44. The IFS Green Budget examined recent housing market trends in detail. It found that:

The evidence we have been able to gather does not suggest that the features of a housing bubble are present to any great extent in the UK housing market as a whole. In particular, both nominal and real prices are still below both their previous peaks and the levels that would be predicted by longer-term trends.⁷⁹

However, it highlighted the market in London as a “particular focus of concern”:

the distinct aspects of activity in this market—the proximity of nominal prices to their 2007 peak, a rising as opposed to stable ratio of house prices to earnings (and, in fact, rising faster than its long-run trend would suggest), and the rising number of high mortgage offers relative to income—indicate that the likelihood of a bubble is greatest in London, and they warrant careful monitoring.⁸⁰

45. Mr Chote agreed that there were “some bubbly components to what is going on in the housing market in particular parts of the country perhaps rather more than generally”.⁸¹ The OBR, which makes a long-run assumption that house price inflation follows the rate of household income growth,⁸² forecasts that house price inflation peaked at a rate of 9.2 per cent at the end of 2013, and will fall back to rate of 3.7 per cent by the start of 2017.⁸³ Prof Nickell has previously appeared to question this empirical link between house price growth and income growth, telling us that “[...] the ratio of house prices to disposable income [...] is a number that has been rising by nearly 1 per cent a year for the last 40 years”.⁸⁴ However, he recently told us that:

The house price to income ratio has been growing for the last 40 years, but in some sense that cannot go on forever; otherwise everything you consume would be housing and there would be nothing else left. In other words, housing cannot go on rising as a proportion of expenditure. When we think about the long run, we would turn that off rather than assuming that just goes on and on because we know it cannot go on and on forever.⁸⁵

46. In identifying emerging signs of a bubble, the IFS Green Budget discussed two approaches: firstly, determining the ‘appropriate’ trajectory of house prices and testing whether the actual prices deviate from this; or alternatively, investigating whether house

78 Q142

79 Institute for Fiscal Studies, [Green Budget](#), February 2014, p.110

80 Institute for Fiscal Studies, [Green Budget](#), February 2014, p.110

81 Q142

82 OBR, [Economic and Fiscal Outlook – March 2014](#), p.61

83 OBR, Economic and Fiscal Outlook – March 2014, [charts and tables data](#), Chart 3.13

84 Oral evidence taken before the Treasury Committee, Budget 2013, Q326

85 Q146

purchasers are reporting that they are buying primarily for capital gain.⁸⁶ When asked what principal indicators of a housing bubble were, the Chancellor had a different view:

I think you would look at headline house prices across the country and, as I say, try to separate out the central London phenomenon from what is going on around the country [...] So you look at the overall levels of house prices, the sustainability of household debt and I guess you look at housing starts. Those are all issues you would want to keep your eye on.⁸⁷

47. Even in the absence of a bubble, house prices may continue to increase if rising demand is not met with a strong response in supply. Mr Chote said that housing supply was “very unresponsive” to demand.⁸⁸ Although residential construction has increased, with housing starts 23 per cent higher in 2013 than 2012, the IFS Green Budget noted that the near-term prospects for supply remain weaker than they were before 2008:

Although the total quantity of dwellings with planning permission that are yet to begin construction is large (184,000 units in England and Wales, compared with 115,000 new-build completions in England in 2012), it is smaller than it was before 2008. This raises doubts as to whether there will be a faster supply response than in previous periods.⁸⁹

48. The Chancellor announced in his Budget speech that he had “asked the [Financial Policy] committee to be particularly vigilant against the emergence of potential risks in the housing market”.⁹⁰ The remit and recommendations for the FPC, published on the same day as the Budget, do not appear to require any additional vigilance, compared to what was being exercised before; rather, they endorse existing levels of vigilance:

Although housing activity remains below long-term trends, the FPC is right to remain vigilant as the recovery progresses [...] The FPC has also provided important clarity to markets and households about the suite of tools at its disposal to address housing market risks should they emerge in the future.⁹¹

When asked about house price inflation, the Chancellor said:

I say we have to be vigilant. I think we have to keep a close eye. Clearly house prices have started to rise, but that is why we have created the Financial Policy Committee and there is, of course quite a regional variation in this.⁹²

49. The FPC’s statutory responsibility is the “identification of, monitoring of, and taking of action to remove or reduce, systemic risks with a view to protecting and enhancing the

86 Institute for Fiscal Studies, [Green Budget](#), February 2014, p.101

87 Q403

88 Q142

89 Institute for Fiscal Studies, [Green Budget](#), February 2014, p.100

90 [HC Deb 19 March 2014 c783](#)

91 HM Treasury, [Remit and recommendations for the Financial Policy Committee](#), 19 March 2014, p.2

92 Q398

resilience of the UK financial system”.⁹³ Mr Wood pointed out that house prices were a concern to the FPC only to the extent that they affected financial stability:

I think the key thing is that it does not seem to me, from what has been said, that they see controlling house prices per se as part of their remit. Their remit is to control financial stability, so if house prices crashed but banks had a lot of capital put aside to protect them from that crash then that is fine. Of course, for the whole economy a big house price crash, and certainty for households who are affected, is not fine.⁹⁴

In a written briefing, he added that the FPC’s primary means of mitigating financial stability risks from the housing market was to require banks to hold more capital, “rather than attempting the impossible task of stopping house prices rising”.⁹⁵

50. By some estimates, the gap between house prices in London and the rest of the country has reached a record level.⁹⁶ The Chancellor said that it was important to draw a distinction between developments in other parts of the country and “some of the phenomena you see in central London, which are caused by international money and the like coming into central London property.”⁹⁷ Mr Chote said that price growth at the “top end” in London “is not mortgage driven. It is overseas buyers and so on.”⁹⁸ The IFS Green Budget also noted the role of foreign cash buyers in “prime London areas”, but added that the data in this area was “relatively poor”.⁹⁹ The latest Bank of England Financial Stability Report also pointed out the prevalence of foreign buyers in “prime central London”, but added that taking the London market as a whole “they appear to have accounted for only a small share of the London market—around 3 per cent of all transactions, according to some estimates.”¹⁰⁰

51. Regional housing market developments have only a limited bearing on the FPC’s remit and competence. In evidence to the Committee, Dr Mark Carney, the Governor of the Bank of England, said that developments confined to a particular region were unlikely to have implications for the UK’s financial stability:

Stewart Hosie: [...] You would not be able to change LTI or LTV for a certain group of borrowers or even for a certain geographic location, would you?

Dr Carney: Put in the broadest terms, no. Again, to have financial stability implications for the United Kingdom economy it is highly unlikely that a single geographic location, as important as all of them are, would in and of itself create that scale of risk.¹⁰¹

93 [Bank of England Act 1998](#), Section 9C (2)

94 Q21

95 Berenberg Bank, [UK Macro Update: Is the BoE getting nervous?](#), 28 March 2014

96 Financial Times, [London-regional house price gap at record](#), 2 April 2014

97 Q398

98 Q147

99 Institute for Fiscal Studies, [Green Budget](#), February 2014, p.109

100 Bank of England, [Financial Stability Report, November 2013](#), p.23-24

101 Oral evidence taken before the Treasury Committee, Bank of England November 2013 Financial Stability Report, HC (2013-14) 987, Q29

52. When asked about the balance of accountability for stopping house price bubbles, the Chancellor said that “Government and Parliament are accountable for housing supply [...] the FPC have the tools given to it by Parliament to deal with issues like mortgage standards”.¹⁰²

53. The 2004 Barker Review of Housing Supply places some responsibility for housing costs in the hands of Government; its first recommendation states that “Government should establish a market affordability goal [...] to reflect housing as a national priority”.¹⁰³ It argues that the UK’s history of booms and busts “has contributed to macroeconomic volatility, creating a more difficult environment for businesses and for economic policy makers”.¹⁰⁴ As well as making further recommendations relating to housing supply, the Review noted that “tackling issues of macroeconomic stability may also require measures to address the demand for housing. Demand side measures, such as the reform of property taxation could help to mitigate house price cycles”.¹⁰⁵

54. House price and commercial real estate bubbles are easy to spot in retrospect. The problem for the Financial Policy Committee is to spot them in advance of their bursting and take whatever action is required to mitigate their negative effects on financial stability.

55. Wider economic concerns are the responsibility of the Government and the Monetary Policy Committee. The Government is also responsible for fiscal and policy tools which directly influence the housing market. It should therefore state what indicators it believes are most important in detecting any wider economic risks arising from the housing market. It should also set out how it plans to address these risks, should they arise.

56. The Chancellor has asked the FPC to be “particularly vigilant against the emergence of potential risks in the housing market”. It is not clear precisely what this means in practice, since the new remit document endorses the existing levels of vigilance. The Chancellor should provide a more detailed explanation of his comment, and whether he expects the FPC to interpret its remit in a way that might prompt it to take further action as a consequence.

Productivity and the output gap

57. Productivity—the output produced for a given quantity of inputs—has failed to recover in line with output. In particular, labour productivity, measured by output per hour worked, was 4.3 per cent below its pre-crisis peak in the final quarter of 2013,¹⁰⁶ while GDP was just 1.4 per cent below peak.¹⁰⁷ The weakness in productivity has been manifested in a stagnation of real wages.

102 Q401

103 Kate Barker (2004), Review of housing supply—final report, p131

104 Kate Barker (2004), Review of housing supply—final report, p3

105 Kate Barker (2004), Review of housing supply—final report, p6

106 ONS, Labour Productivity, Q4 2013, dataset series [LZVB](#)

107 ONS, Quarterly National Accounts, Q4 2013, dataset series [ABMI](#)

58. Other things being equal, productivity growth serves to offset additional demand for new workers as the economy recovers. The weakness in productivity has consequently contributed to a very strong labour market picture, with employment growing by two million over the past two years, and the unemployment rate falling from 8.3 per cent to 7.2 per cent.¹⁰⁸

59. The OBR's forecast is underpinned by a gradual revival in productivity. Labour productivity in particular is expected to grow by 1.3 per cent in 2014, and by more than 2 per cent in subsequent years.¹⁰⁹ This drives the rising real incomes that in turn provide the basis for sustained household spending growth. Mr Chote said that a pick-up in productivity was crucial for the sustainability of the recovery:

Absolutely central to the durability of the recovery is an improvement in the productivity position, and with that a return to sustainable real income growth and, therefore, a sustainable path for consumption¹¹⁰

60. The OBR acknowledges that “productivity has been exceptionally weak in the recent past”¹¹¹ and Mr Chote said that economists were little closer to understanding the causes of this.¹¹² He also said that the OBR had “been waiting for this pick-up in productivity growth to come for some time”, adding that “if you are asking for one single question mark over sustainability, that is probably the score.”¹¹³

61. The failure of productivity to grow in line with output during the recovery has meant that, in the OBR's judgement, “the unexpected strength of GDP growth over the past year [has] been largely cyclical”;¹¹⁴ in effect, that recent growth has not been associated with an increase in the economy's supply capacity. The corollary of this judgement is that the OBR's estimate of the output gap in 2013—the difference between actual and potential output—was revised down from 3.8 per cent to 1.7 per cent between its March 2013 and March 2014 forecasts.¹¹⁵

62. Estimates of the output gap vary considerably between independent forecasters. At the time of the Budget, the range of independent forecasts for the output gap in 2014 varied by 6.6 percentage points: the most optimistic estimated that the economy was operating at 5 per cent below potential; the most pessimistic estimated it was operating at 1.6 per cent above potential.¹¹⁶

63. Despite the uncertainty about its size, or even whether it is positive or negative, the output gap has crucial implications for judging performance against the fiscal mandate,

108 ONS [Labour Market Statistics, March 2014](#), reference tables A01

109 OBR, Economic and Fiscal Outlook – March 2014, [supplementary economy tables](#), Table 1.6

110 Q148

111 OBR, [Economic and Fiscal Outlook – March 2014](#), p.40

112 Q150

113 Q114

114 OBR, [Economic and Fiscal Outlook – March 2014](#), p.12

115 OBR, Economic and Fiscal Outlook, March 2013, [charts and tables data](#), Chart 3.7; Economic and Fiscal Outlook, March 2014, [charts and tables data](#), Chart 3.23

116 OBR, Economic and Fiscal Outlook, March 2014, [charts and tables data](#), Chart 3.6

since it determines how much borrowing is a result of temporary, rather than structural, factors. However, the OBR and the Bank measure the output gap on a different basis. Mr Chote clarified the distinction and the reasons for it:

The obvious reason for the distinction is basically the time profile over which we are looking. The Bank of England is obviously concerned about what is driving inflation over a policy horizon of two to three years or thereabouts. We are looking at a longer five-year horizon. For example, I think an obvious distinction is what, in the long term, do you believe is the sustainable rate of unemployment that would be consistent with keeping inflation stable. There, in the long term, the Bank and we have fairly similar views, that the long-run sustainable rate of unemployment is probably about 5 per cent and a bit [...] We are [currently] in the position where we have roughly the same answer but to two different questions.¹¹⁷

64. The OBR judges that the potential rate of GDP and productivity growth will eventually return to a rate consistent with historical trends, but that this will not happen before the end of its forecast period.¹¹⁸ Mr Chote said that this was “simply by virtue of the fact that we have no better basis upon which to make a long-term judgement”, adding that “there is no reason to think that the financial crisis should have affected the long-term growth rate of potential GDP or long-term underlying productivity performance”.¹¹⁹ Professor Nickell added that “aside from the world wars, this [trend rate] has been going on for 100 years and it is very hard to argue that we are in a new regime”.¹²⁰ However, the OBR acknowledges that there are alternative views and significant uncertainty surrounding this judgement:

Some believe the financial crisis of 2008 coincided with a permanent slowdown in productivity growth, perhaps reflecting the exhaustion of ‘low-hanging fruit’ efficiency gains in the IT sector. Others are more optimistic, assuming efficiency gains have continued apace but that weak demand is masking the process.

Our central judgement lies between these two views. We expect productivity growth to return to its historical average as the pace at which resources are reallocated to more productive uses picks up, but with the level of productivity, and therefore per capita GDP, permanently lower relative to its pre-crisis trend. This judgement is subject to significant risks in both directions.¹²¹

65. The evidence we took concurred with the view of the OBR that the recovery to date has been driven by an increase in demand without a corresponding rise in supply potential. The output gap is being reduced in size and, so far, there is insufficient evidence to support the view that productivity growth is returning.

117 Q105

118 OBR, [Economic and Fiscal Outlook – March 2014](#), p.40

119 Q154

120 Q155

121 OBR, [Economic and Fiscal Outlook – March 2014](#), p.40

3 The public finances

Performance against the fiscal targets

66. The Government's fiscal targets are set out in the Charter for Budget Responsibility. At the Budget, the Government amended the existing Charter to account for changes related to the introduction of the welfare cap. The Government's fiscal targets, as originally set out in 2010, were not changed.¹²²

67. The Government has set itself two medium-term fiscal targets: the fiscal mandate and the supplementary target. The fiscal mandate is to target a “cyclically adjusted current balance by the end of the rolling, five year fiscal period”, whilst the supplementary target is for “public sector net debt as a percentage of GDP to be falling at a fixed date of 2015–16”.¹²³

Table 2: Changes to the cyclically-adjusted current budget since December 2013

	Per cent of GDP						
	2012–13	2013–14	2014–15	2015–16	2016–17	2017–18	2018–19
December forecast	-3.6	-2.9	-2.0	-1.4	-0.2	0.7	1.6
March forecast	-3.5	-2.8	-2.2	-1.5	-0.2	0.7	1.5
Change	0.2	0.1	-0.2	-0.2	0.0	0.0	0.0

Source: Office for Budget Responsibility, *Economic and fiscal outlook, March 2014*, p 167

Table 3: Changes to public sector net debt projections since December 2013

	Per cent of GDP						
	2012–13	2013–14	2014–15	2015–16	2016–17	2017–18	2018–19
December forecast	69.9	74.4	78.3	80.8	81.2	80.0	77.6
March forecast	70.1	73.6	77.5	79.8	79.8	78.1	75.7
Change	0.2	-0.8	-0.8	-1.0	-1.4	-1.9	-1.9

Source: Office for Budget Responsibility, *Economic and fiscal outlook, March 2014*, p 166

68. The OBR's March 2014 Economic and Fiscal Outlook forecasts the cyclically adjusted current budget to be in surplus by 1.5 per cent of GDP in 2018–19, with a surplus of 0.7 per cent in 2017–18. The OBR therefore forecasts that the Government will meet its fiscal mandate a year early.¹²⁴ However, public sector net debt is forecast to rise by 1.5 percentage points in 2015–16, and not fall until 2016–17. As a result, the Government is forecast to miss its supplementary target by one year.¹²⁵

122 HM Treasury, Budget 2010, June 2010, [HC 61](#), p 12, paras 1.15-1.16

123 HM Treasury, [Charter for Budget Responsibility, March 2014 update](#), 19 March 2014

124 Office for Budget Responsibility, [Economic and Fiscal Outlook – March 2014](#), 19 March 2014, p 167, table 5.2

125 Office for Budget Responsibility, [Economic and Fiscal Outlook – March 2014](#), 19 March 2014, p 167, para 5.9

69. In the latest Budget, the Government opted for a fiscally neutral stance.¹²⁶ This is in line with statements made at the 2012 Autumn Statement, where the Chancellor of the Exchequer noted that the Government was not pursuing the supplementary target:

One of the central judgments of this Autumn Statement was not to chase the debt target, in other words, to accept that we had missed the debt target, and had we chased the debt target, that would have required significant cuts or tax rises over the next couple of years.¹²⁷

As a result, the OBR has forecast that the Government will not meet the supplementary target. In June 2012, the IFS told us that the Government would effectively “be putting more than an additional £100 billion into the economy in the years 2012–13 to 2014–15 than it had planned”.¹²⁸

70. For the fourth Economic and Fiscal Outlook in a row, the OBR forecasts that the Government will meet the rolling fiscal mandate, but not the supplementary target. In line with previous occasions, the Government has not proposed any corrective action in order to meet the supplementary target. Instead the Government has allowed the automatic stabilisers to continue their work, rather than taking corrective action—tightening fiscal policy—in order to meet the supplementary target.

Changes announced in the Budget

71. The overall effect of policy changes announced in the Budget was broadly fiscally neutral, with a small net positive impact on the public finances of £150 million over the five year forecast period. The Government said in the Budget:

Reflecting the government’s commitment to responsible fiscal policy, and despite the improved borrowing forecast by the OBR, Budget 2014 sets out a fiscally neutral response with the improvement in the fiscal forecast helping to return the public finances to a sustainable position.¹²⁹

Table 4: Summary of Budget policy decisions

	£ million				
	2014–15	2015–16	2016–17	2017–18	2018–19
Total tax policy decisions	-10	-640	-1,800	-1,420	-1,685
Total spending policy decisions	-540	+80	+2,025	+2,055	+2,085
TOTAL POLICY DECISIONS	-550	-560	+225	+635	+400

Source: HM Treasury, Budget 2014, 19 March 2014, p 57, Table 2.1

72. Of the 54 policy changes announced, seven are projected to cost or raise more than £1 billion in total over the forecast period:¹³⁰

126 HM Treasury, Budget 2014, 19 March 2014, p 20, para 1.52

127 Oral evidence by the Chancellor of the Exchequer to the Treasury Committee, Autumn Statement 2013, 13 December 2013, Q 290

128 Letter from Paul Johnson, Director, IFS, 13 June 2012

129 HM Treasury, Budget 2014, 19 March 2014, p 20, para 1.52

130 HM Treasury, Budget 2014, 19 March 2014, p 56–57, table 2.1

- The increase in the personal allowance to £10,500 in 2015–16 with equal gains to higher rate taxpayers
- Reduction in the tax rate for pension withdrawals to the marginal income tax rate
- Abolition of the 10 per cent rate for saving, and an increase in the 0 per cent band to £5,000
- Equalising stocks and shares and cash ISA limit, with an increase in the annual limit to £15,000
- Increase of the annual investment allowance to £500,000
- Limiting carbon price floor disparity between the UK and EU
- Accelerated payment of disclosed tax avoidance schemes and the General Anti-Abuse Rule.

73. The OBR noted that some of the measures announced at the Budget had “markedly different implications beyond the five year scorecard period than within it”.¹³¹ In particular, the Treasury provided longer term revenue consequences for four of the measures:

- the pension withdrawals measure, which brings forward income tax receipts but has a small steady-state cost in the long term;
- voluntary NICs, which increases NICs receipts in the short term but also increases long-term state pension costs;
- the temporary annual investment allowance increase, which raises the amount of tax relief that can be claimed until December 2015, but then reduces it thereafter, largely recouping the scorecard costs; and
- accelerated payments related to tax avoidance schemes, which brings forward receipts from future years.

74. The long run effects of the four measures above are presented in chart 4. Commenting on the effects, the OBR said:

The net effect of these measures is to increase receipts over the scorecard horizon by £1.2 billion a year on average, but the revenue raised then drops sharply in 2019-20 and averages only £0.2 billion a year over the 15 years beyond the scorecard horizon. Given the uncertainty associated with costing these policy measures over a 5-year horizon, the longer-term implications will be also be subject to considerable uncertainty.¹³²

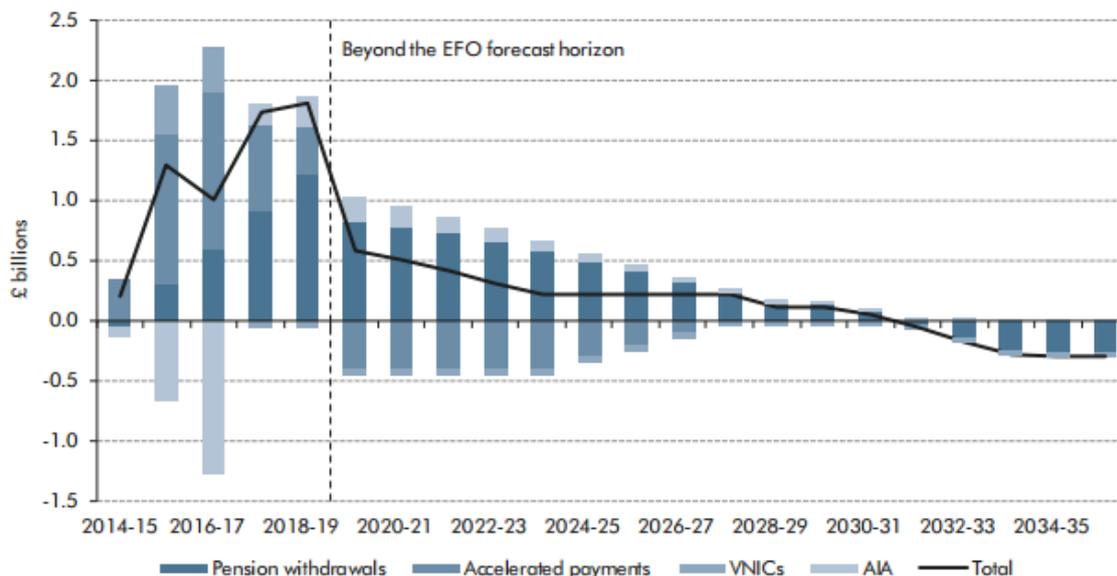
131 Office for Budget Responsibility, [Economic and Fiscal Outlook – March 2014](#), 19 March 2014, p 97, para 4.27

132 Office for Budget Responsibility, [Economic and Fiscal Outlook – March 2014](#), 19 March 2014

75. Commenting on these measures, the IFS noted that “permanent tax giveaways” set out in the Budget were being paid for by “temporary increases in tax revenues”.¹³³ Paul Johnson, Director the Institute for Fiscal Studies, said:

These things balance out in the scorecard but the increased revenue runs out pretty soon after the end of the scorecard, and indeed goes negative, while the reduced taxes or increased spending are permanent. Obviously they can be changed but it is more difficult to change these things once they are there.¹³⁴

Chart 4: Revenue raised by selected Budget policy measures



Source: Office for Budget Responsibility, *Economic and Fiscal outlook*, 19 March 2014, p 98, chart 4.1

76. However, compared to the overall size of the Government finances, these measures are relatively small. Mr Johnson noted that “these are a few billions out of the still £100 billion-odd of borrowing we are doing.”¹³⁵ He also noted that the estimates of revenue and expenditure arising from the measures were highly uncertain:

The scorecard suggests an extra £1 billion or £1.5 billion of revenues in the short run. The OBR document makes it very clear there is a huge amount of uncertainty about that and that depends on fairly unknown assumptions about how pensioners will behave: how much they will draw down early or the extent to which they will, nevertheless, buy annuities or not. If you take those forecasts, in the long run—and I think this is after about 2030-something—you get a reduction in revenues as the income is used up a bit quicker. I think the answer is the fiscal implications are probably small; probably positive in the short run and negative in the long run.¹³⁶

133 Institute for Fiscal Studies, “Economy bouncing back more strongly but policy choices have increased long-run risks to the public finances,” 2014 post budget briefing slides, 20 March 2014

134 Q52

135 Q52

136 Q61

77. Mr Johnson said that overall the Chancellor was “not being quite as prudent as [he] might suggest”, and that he did not believe it was “an entirely neutral Budget.”¹³⁷ Mr Johnson also warned that this was not the first time he had seen short term revenue increases in the Budget:

One reason for stressing that a little more than we might otherwise is that rather similar things have been done over the last budget and autumn statement where we have seen, for example, one of the biggest, contracting out for employer national insurance contributions, will cost the public sector around £3 billion a year. That was scored as additional revenue and the assumption is that they will just be additional spending cuts. It is something that has happened two or three times. You begin to add those up and it begins to make a noticeable difference.¹³⁸

78. The Budget was fiscally neutral on a five year view—the forecast period. Four of the measures announced have consequences within the forecast period that differ significantly from their longer term effects. These measures are fiscally positive within the five year forecast period. However, this tapers and they are projected to be fiscally negative after 20 years. While the effect of these four spending decisions may be small, and subject to uncertainty, the Committee would be concerned if the Government made fiscal decisions with its eye only on the five year forecast period. It is important that the OBR cost the long term implications of Budget measures.

Cyclically adjusted current budget

79. The Government’s fiscal mandate is “a forward-looking target to achieve cyclically-adjusted current balance by the end of the rolling, five-year forecast period”.¹³⁹ According to the OBR, this means that “total public sector receipts need to at least equal total public sector spending (minus spending on net investment) in five years’ time, after adjusting for the impact of any remaining spare capacity in the economy.”¹⁴⁰

80. The OBR’s methodology for adjusting for the impact of spare capacity on the public finances is set out in its working paper *Cyclically adjusting the public finances*.¹⁴¹ The OBR’s approach relies heavily on its estimation of the size of the output gap. As already noted, the output gap is unobservable and very difficult to estimate. As the OBR has said:

Past experience and common sense suggest that there are significant upside and downside risks to our central forecasts for the public finances. These reflect uncertainty both about the outlook for the economy and about the level of receipts and spending in any given state of the economy.¹⁴²

In the Economic and Fiscal Outlook, the OBR noted that it had judged the size of the output gap to have been larger than its own cyclical indicators—a method of estimating the

137 Q53

138 Q53

139 HM Treasury, [Charter for Budget Responsibility, March 2014 update](#), 19 March 2014

140 Office for Budget Responsibility, [Economic and Fiscal Outlook – March 2014](#), 19 March 2014, p 165, para 5.3

141 Office for Budget Responsibility, “Cyclically adjusting the public finances”, June 2012

142 Office for Budget Responsibility, [Economic and Fiscal Outlook – March 2014](#), 19 March 2014, p 169, para 5.14

size of the output gap—had suggested. According to Mr Chote, the cyclical indicators suggested that the size of the output gap was around two percentage points smaller.¹⁴³

81. The Committee asked both Mr Chote and Graham Parker, a member of the Budget Responsibility Committee, how a smaller estimate of the output gap would affect the CACB. Both agreed that it would have worsened the cyclically adjusted fiscal position by around £20 billion.¹⁴⁴ When asked whether whether this would have led to the need for additional fiscal tightening to meet the fiscal mandate, Mr Chote said that he did not know, but that “it would be quite close.”¹⁴⁵ He also said:

I suspect, if you took [the cyclical indicators] completely at face value, we would be at the very small end of the spectrum and it would use up most of the room for manoeuvre against the mandate.¹⁴⁶

Mr Chote also commented on longer term uncertainty in the CACB:

I am sure, if [the government] were here, they would say that they believe that delivering a sustainable medium-term fiscal path does help deliver your broader economic objectives. I think the key point to bear in mind is that, as you say, you do not know with confidence what the output gap is going to be at that sort of horizon, which is one reason why, in every forecast that we have produced, we do a sensitivity analysis to show how wrong you have to be about that in order for the rule to be in danger of being breached.

The other uncertainty, of course, even if you know what the activity is, is whether you get the forecast of the unadjusted deficit right over that horizon. Clearly that is not straightforward either, so you have two sources of difficulty there.¹⁴⁷

82. The Government is planning to update its fiscal mandate later this year. The Committee asked IFS witnesses whether the cyclically adjusted current budget should remain part of the fiscal mandate. Mr Johnson said:

It is a difficult one. I think it is appropriate to think about your fiscal position in the context of where you think you are relative to the cycle or relative to the output gap. Clearly, if you are simply outbalanced, if you think you have a massive negative output gap, you are well above trend, then that is not a long-term sustainable position. [...] but there are balances between uncertainty on the one hand and the need to have an output gap measure on the other.¹⁴⁸

Gemma Tetlow, Programme Director at the IFS, made a further point, noting that the current significant distinctions between unadjusted and cyclically adjusted measures were particularly acute due to the depth of the recent recession:

143 Q185

144 Q186

145 Q187

146 Q185

147 Q189

148 Q54

The only thing I would add to that is, as Paul said, there are good reasons for not worrying about the bits of borrowing that are purely cyclical and temporary. In more normal times, this distinction becomes less important. If you are in a small recession or you are in a small boom, then well within the five-year forecasting horizon you would expect the economy to be back at its trend level again and, therefore, the cyclically-adjusted measure is exactly the same as the headline measure. The reason that the cyclically-adjusted measure was an important part of the fiscal mandate four years ago now is that we were forecasting a very long period of below potential economic activity. Therefore, there was a difference for all five years of the forecast horizon between a cyclically-adjusted measure and a headline measure. As we get back to a more normal operating position, I think the distinction between the two becomes a lot less important and it is a lot easier simply to think about the headline measure.¹⁴⁹

Mr Chote of the OBR said:

You can clearly have a target that is not a cyclical one and, at one level, that is simple. The Chancellor has suggested he would like to be in a situation where you are looking for a simple, straightforward surplus on the overall budget. That is clearly easier to understand and to interpret than a cyclically-adjusted surplus or balance on the current budget.¹⁵⁰

83. After an economic shock, cyclically adjusted measurements are particularly uncertain. The current fiscal mandate is dependent on an unobservable output gap. It has been made even more unreliable as a consequence of the financial crisis.

84. For most of the last 30 years, governments have been trying to devise a robust fiscal anchor. There have been successive Medium Term Financial Strategies; the Code for Fiscal Stability (modified during the crisis by the temporary operating rule); and the Charter for Budget Responsibility. The Government is now considering a new Charter for Budget Responsibility. Fiscal anchors have merit. But at a time when the credibility of pledges in all aspects of public policy has attracted greater scepticism than before, it will be more difficult to build confidence in the fiscal anchor deep enough to withstand an extreme event.

Ring fencing

85. The Government has been following a policy of ‘ring fencing’ certain departmental budgets. In the 2013 Autumn Statement, the Government confirmed that expenditure on Health, schools and Official Development Assistance (ODA) would “be protected in line with the policy set out at Spending Round 2013”.¹⁵¹ No change to this policy was announced in the Budget.

86. The Committee has already expressed concern about the long term impact of ring fencing on the shape of Government, particularly if departmental spending were to be cut

149 Q54

150 Q191

151 HM Treasury, Autumn Statement 2013, Cm 8747, December 2013, p81, para 2.7

further than it has been already. The IFS in its Green Budget 2014 noted the implications of ring-fencing on allocations of departmental spending: “By 2015–16, while total departmental spending will be 11.1% lower than in 2010–11, departmental spending on areas other than the NHS, schools and aid will have been cut by 21.0%”.¹⁵² The Committee’s Autumn Statement 2013 report said:

Ring fencing, by definition, requires that the balance of public expenditure restraint and cuts be borne in the rest of public expenditure. Each successive year of public expenditure restraint results in an increase in ring-fenced spending as a proportion of the total. The smaller non-ring fenced areas in turn have to bear a higher proportion of any savings in subsequent years. The IFS has shown that non-ring-fenced expenditure may fall from 61.6 per cent in 2010–11 to around 50 per cent in 2018–19 of total Departmental Expenditure Limits. Ring fencing also reduces the discipline on spending in these areas: the rigour of negotiations between the department and the Treasury on allocations will be weakened, since it is known in advance by both sides that this spending is protected.¹⁵³

87. In its fiscal plans for the period 2015–16 to 2018–19, the Government has set a fiscal envelope that requires further fiscal consolidation. Witnesses told the Committee that the further fiscal tightening planned during the next Parliament would be significant in scale. Mr Saunders said:

In broad terms if you go back to the 2010 budget, about 90 per cent of the total fiscal tightening in terms of the structural primary balance would have been completed by the end of the fiscal year that is about to begin, the 2014–15 year, before the next election. Ever since then that proportion has fallen steadily and under the current plans it is about 50:50. The total fiscal tightening is just above 10 per cent of GDP and roughly 5 per cent of GDP of that happens in this Parliament, most of it in the first two years, and roughly 5 per cent of GDP is pencilled in for the next Parliament. [...] We have lifted a headwind, if you like.¹⁵⁴

Ms Tetlow expanded on this point, noting:

If you think instead about what active policies have been introduced and are placed, the current Coalition Government has stuck to its plan for the tax increases and the spending cuts it was going to do in this Parliament but, in a sense, the size of the problem that they have been faced with has been revised over time. They have tacked on to the end of it additional cuts to come in the next Parliament.¹⁵⁵

88. The Government has announced the spending envelope for 2015–16 to 2018–19, but the areas where spending will be reduced, or income raised, have not yet been set out in detail by the Government. Mr Johnson said:

¹⁵² IFS, Green Budget 2014, 5 February 2014, p40

¹⁵³ Treasury Committee, “Autumn Statement 2013,” HC 826, p 28, para 45

¹⁵⁴ Q25

¹⁵⁵ Q59

Beyond 2015–16 we have not heard from this Government what exact spending cuts they would introduce. We do not know what the Opposition would do. That is kind of the position we were at in 2009–10 before the election, but clearly [...] there are three years of very big spending cuts pencilled in and we know next to nothing about what they will look like.¹⁵⁶

89. Ring fencing distorts spending decisions. It also weakens rigorous scrutiny of spending in ring fenced departments. Furthermore, with each year that ring fencing remains in place, the size of ring fenced departments increases as a proportion of total departmental spending. The IFS has stated that by 2015-16, expenditure reductions of 21 per cent will have been implemented in areas other than the NHS, schools and overseas aid. Each successive round, seeking reductions from an already smaller non-ringfenced base, will be more difficult than its predecessor.

Welfare cap

90. The 2014 Budget set out the Government’s additional controls over annually managed expenditure (AME) on welfare—the welfare cap. The welfare cap is a cap on forecast welfare spending. It is not a cap on actual welfare spending. The Government states that the welfare cap “will not apply to the first year of the forecast horizon, or to years previous to the first year of the forecast horizon.”, and that “The welfare cap and margin will roll forward every year. The level of the welfare cap for the additional year will be published at the same time as the level of the margin”.¹⁵⁷

91. The level of the cap has been set for the years 2015–16 to 2018–19 at the level of the OBR’s forecast, and consequently the Government’s existing spending plans, as published in the March 2014 Economic and Fiscal Outlook.¹⁵⁸

Table 5: The level of the welfare cap and the forecast margin

	£ billion			
	2015–16	2016–17	2017–18	2018–19
Welfare cap	119.5	122.0	124.6	126.7
Forecast margin (2%)	2.4	2.4	2.5	2.5

Source: HM Treasury, Budget 2014, 19 March 2014, p 26, Table 1.5

92. Rules governing the cap are set out in an updated Charter for Budget Responsibility published alongside the Budget. These rules include: how the cap is to be set; how and when the size of the cap can be changed; the requirement for a forecast margin above the cap; how the cap is to be assessed; how the contents of the cap can be changed; under what circumstances the cap is considered to be breached; and actions to be taken by the Government in the event of a breach.¹⁵⁹

156 Q59

157 HM Treasury, [Charter for Budget Responsibility, March 2014 update](#), 18 March 2014, paras 3.21-3.24

158 HM Treasury, Budget 2014, 19 March 2014, p 26, para 1.76

159 HM Treasury, [Charter for Budget Responsibility, March 2014 update](#), 19 March 2014

93. The OBR will assess the Government's adherence to the welfare cap in every autumn Economic and Fiscal Outlook. Alongside this will be a new report from the OBR on welfare trends, published annually.¹⁶⁰ The OBR's autumn EFO analysis will be updated in every Budget EFO, but no formal assessment will take place.¹⁶¹

Effect on policymaking

94. The stated aim of the welfare cap is to “improve spending control”.¹⁶² The cap is breached if either “spending within its scope is forecast to increase above the level of the cap in any year in which it applies, as a result of discretionary policy action” or if “spending is forecast to increase above the margin in any year where the cap applies, for any reason.”¹⁶³

95. A breach of the cap triggers “a debate on a voteable motion led by the Department for Work and Pensions, normally within 28 sitting days.” The Department for Work and Pensions will then have three options: to propose Government policy measures which will reduce welfare spending to within the level of the cap; to seek approval for the level of the welfare cap and/or margin to be increased, along with an explanation of why this is considered to be justified; or to explain why a breach of the welfare cap is considered justified.¹⁶⁴

96. There has in recent years been an increasing tendency for government targets to be given a statutory underpinning. Examples of such “declaratory legislation” include the fuel poverty target set by the Warm Homes and Energy Conservation Act 2000, targets to reduce greenhouse gas emission, set by the Climate Change Act 2008, and targets for the reduction of child poverty, set by the Child Poverty Act 2010. Commenting on the likely effectiveness of the welfare cap, Mr Johnson noted that previous government targets of this kind, including the child poverty target and the supplementary debt target, had not been met. He said that targets enshrined in legislation “do not appear to have had an enormous amount of bite”,¹⁶⁵ and noted that their deterrent effect generally amounted to “political stigma”. He added: “Sometimes that works and sometimes it does not.”¹⁶⁶ Moreover, Mr Johnson warned that the cap would come under much more pressure during a recession, when it would be more likely to be abandoned:

[...] if we did fall into some significant additional recession—and we know that, while the Job Seeker's Allowance and particular bits of housing benefit are clearly driven by the cycle, other bits of the benefit system are not invariable to the cycle and might rise in the circumstances that you are describing. The question is—and I do not know the answer to this question—suppose that were to happen, would this cap bite or is this a cap only for normal times? I presume that the Chancellor will say this

160 Office for Budget Responsibility, Economic and Fiscal Outlook, 19 March 2014, para 4.141

161 Office for Budget Responsibility, Economic and Fiscal Outlook, 19 March 2014, para 4.139

162 HM Treasury, Budget 2014, 19 March 2014, p 26, para 1.76

163 HM Treasury, [Charter for Budget Responsibility, March 2014 update](#), 19 March 2014, p 10, para 3.30

164 HM Treasury, [Charter for Budget Responsibility, March 2014 update](#), 19 March 2014, p 10, para 3.31

165 Q77

166 Q77

is a cap for whatever times, but it would clearly bite much harder if we were to move into a substantial recession than under normal circumstances.¹⁶⁷

97. Witnesses did, however, agree that increased scrutiny of welfare spending alongside additional analysis from the OBR on welfare trends could affect and might improve policymaking. Commenting on the impact the cap might have on policymaking in future, Mr Saunders said:

I would guess quite large if it is bought into by all parties because it would mean that you would have a trade-off. If you propose new welfare measures then you would have to squeeze elsewhere.¹⁶⁸

Mr Mortimer-Lee suggested that the cap would “lead to much more political consideration or consideration in society more broadly about how much we spend on these items of welfare.”¹⁶⁹ He added:

For some of the longer-term choices, in a way by focusing on a number I think you are going to bring into sharp relief a choice between welfare spending and spending on current goods and services by Government as we come to future consolidation because people are going to say, “Some of the departmental spending is going to be cut by 30%-odd. Shouldn’t we cut the welfare budget?”¹⁷⁰

Ms Tetlow also commented favourably on the impact of increased scrutiny and the OBR’s new report. She suggested that the cap could have a positive effect if budgets had grown unintentionally or unexpectedly:

To the extent that this causes you, on an ongoing basis, to assess where welfare spending is going, and the OBR is, in fact, going to publish a report each autumn assessing changes to the welfare forecast and what is going on. To the extent that it causes you to have an ongoing review of benefit spending and to think about, “What is the level of this and how is it distributed and why has it changed since we last looked at it”, I think that is a positive thing. Hopefully, it might cause you to make better policies because you look at this every year rather than suddenly realising that your budget has exploded in a way you did not intend and then trying to address the issue.¹⁷¹

Design of the cap

98. The Government has set out which elements of welfare sit inside and outside the cap in its latest Budget, describing the cap as containing “all welfare spending in AME, with the exception of the state pension and the automatic stabilisers.”¹⁷² According to the OBR, of

167 Q77

168 Q37

169 Q40

170 Q40

171 Q80

172 HM Treasury, Budget 2014, 19 March 2014, p 27, para 1.78

the £210.1 billion of total welfare spending for 2013–14, £116.4 billion of spending, or approximately 55.4 per cent, sits within the cap.¹⁷³

99. While the Government has stated that the automatic stabilisers are excluded from the cap, some potentially cyclical elements of welfare spending, such as in work credits, remain inside.¹⁷⁴ Commenting on the desirability of limiting such in-work credits, Mr Mortimer-Lee said:

If these individuals have low productivity and therefore would be able to access only a very low wage or no job at all, is it better to subsidise those people to be in a job or should we allow them to be unemployed? My own view is that it would be better for low productivity individuals that we subsidise them and encourage them into employment when otherwise they might not be employed. I think that has lots of desirable social consequences and there is also a strong argument for encouraging that to build up experience and human capital over a period.¹⁷⁵

[...]

If you take a much more puritan point of view, they might be unemployed for a very long time and therefore end up with no skills whatsoever. I think that would be a poor outcome for them and for society.¹⁷⁶

100. The Committee also asked for witnesses' opinions on the exclusion of the state pension and automatic stabilisers from the cap. Mr Mortimer-Lee agreed with the exclusion of pensions, and noted that they were elements of spending that were difficult to control:

If you are going to have a cap you should try to cap those things that you can control and don't cap those things that you can't control. In terms of Jobseeker's Allowance, you can't control precisely how many unemployed people there are going to be, so you should not try to control that. To some extent, people's decisions about retirement are also out of it. It may be sensible to start small and then think about where you are going to go over the longer term.¹⁷⁷

Mr Johnson agreed, saying:

It is not clear what the benefit of putting the state pension in would be. The state pension is completely uncontrollable unless you think you are going to renege on previous promises or you are going to adjust, year by year, the rate at which you increase the state pension. If you put the state pension in you are, I think, suggesting that you would consider adjusting the state pension and that is just a policy decision for Government.¹⁷⁸

¹⁷³ OBR, [Economic and Fiscal Outlook – March 2014](#), p 141, table 4.28

¹⁷⁴ HM Treasury, Budget 2014, 19 March 2014, p 27, table A.2

¹⁷⁵ Q41

¹⁷⁶ Q42

¹⁷⁷ Q40

¹⁷⁸ Q75

101. The welfare cap acts as a limit on total welfare spending, but does not impose restrictions on how spending is allocated within the cap. Mr Johnson said that this meant that the cap was “potentially very flexible if different things are going on with different bits of the system, but very inflexible if everything is moving in the same direction.”¹⁷⁹ Commenting on the cap’s design, Mr Johnson said:

You can imagine a world in which one benefit, say personal independence payments, starts rising much quicker than expected but that is offset, for some reason, by some reduction in housing benefit or tax credit. If that happened, the cap would not bite and that would not force any policy change, but you might think that you want to be thinking about each individual benefit and what the appropriate structure and spending on those is.¹⁸⁰

102. Overall, Mr Johnson suggested that the cap was a somewhat blunt instrument, noting that “this is a very top-level cap. It would be very nice to see more detail underneath that about some of the ways in which you might respond.” He said:

Whether you would want to change the rules just because higher levels of low income had resulted in more people coming on to housing benefit; you might want to respond to that differently to where something was going up because rents were rising much more quickly than you expected.¹⁸¹

Forecast margin

103. As noted earlier, the welfare cap is subject to a forecast margin. In practice, this means that the Government will only be deemed to have breached the cap if one of two conditions is met:

- if spending within its scope is forecast to increase above the level of the cap in any year in which it applies, as a result of discretionary policy action; or
- if spending is forecast to increase above the margin in any year where the cap applies, for any reason.¹⁸²

This is intended to prevent inaccuracies in the forecasts of welfare spending triggering the sanctions of the cap, and therefore ensure that “policy action is not triggered by small fluctuations in the forecast.”¹⁸³

104. The Government has set the margin at 2 per cent of projected welfare spending on the categories of spending that fall within the scope of the cap, for each year of the five year forecast horizon, excluding the first one. Commenting on the size of this margin, Ms Tetlow noted that a 2 per cent margin would have been breached in the recent past:

179 Q74

180 Q73

181 Q79

182 HM Treasury, [Charter for Budget Responsibility, March 2014 update](#), 29 March 2014, p10, para 3.30

183 HM Treasury, Budget 2014, 19 March 2014, p 26, para 1.76

We did try to look a little bit at how binding this 2 per cent forecasting margin is and the one time that it would have been breached in the last few years is, between the 2011 budget and the 2012 budget, there was a reasonably significant downgrade in the economic forecast from the OBR. That led to the forecast for welfare and scope spending in 2015 being more than 2 per cent higher in budget 2012 than it was in budget 2011. That was a reasonably significant revision to the economic forecast, but not a large recession. That sort of scale of change could cause a breach in this.¹⁸⁴

Mr Johnson also commented on the size of the forecast margin, noting that the size of the welfare budget becomes progressively less certain nearing the end of the forecast window:

One is that it is interesting looking at the cap and the amount of forecasting room around it, which does not grow as you go out. It is about 2 per cent or 2 per cent-and-a-bit each year into the future. You would expect the uncertainty to grow over time. Potentially at least, the tightness of this cap will be bigger over time or it may turn out to be very loose, because there is quite a lot of uncertainty about where we will be in 2018, for example. I suspect setting it five years ahead with a fixed 2 per cent to 2 per cent-and-a-bit forecasting margin around it will not last.¹⁸⁵

105. 17 per cent of headline total managed expenditure in 2012–13 would have been covered by the welfare cap. The cap raises a number of concerns and we intend to seek further written evidence on its design and operation. Some welfare spending is not included within the cap. This may distort decision making, for example by tempting a government to change welfare entitlements in order to avoid breaching it. The penalty for a breach of the cap is any political embarrassment that may come with Parliamentary debate, a requirement in the event of its breach. The cap is therefore declaratory. Previous examples of such declarations include the child poverty target and the fuel poverty target.

184 Q78

185 Q72

4 Pension reforms and savings

Increasing pension flexibility

Past reforms

106. Over the past twenty years, the previous requirement for retirees to purchase an annuity has been gradually relaxed. In 1995, income withdrawal up to the age of 75 was introduced.¹⁸⁶ This allowed retirees to defer the purchase of an annuity and instead to draw down personal pension savings within specified limits. This was known subsequently as an Unsecured Pension Arrangement (USP).¹⁸⁷

107. The introduction of Alternatively Secured Pensions (ASPs) in 2006 allowed pensioners to draw down funds beyond the age of 75, further relaxing the requirement to purchase an annuity. In 2010, the Government stated that ASPs were not intended to be widely used:

ASPs were introduced to provide an alternative to annuities for people who have principled objections to annuitisation, and were never intended to be widely used as an alternative to annuitisation. Consequently, the existing pensions tax rules effectively require most members of registered pension schemes to purchase an annuity by age 75.¹⁸⁸

108. In 2011, the Government further reformed the operation of income drawdown by introducing a 'two-tier' system: capped and flexible drawdown. Capped drawdown had a withdrawal limit and requirement for triennial reviews before age 75 and yearly reviews after 75. Flexible drawdown permitted withdrawals of any amount subject to ensuring a secure income meeting the minimum income requirement as set by HM Treasury.¹⁸⁹

Immediate changes

109. The Budget announced some immediate changes to the pensions system. It said that, with effect from 27 March 2014, the Government would:

- reduce the amount of guaranteed pension income people need in retirement to access their savings flexibly, from £20,000 to £12,000
- increase the capped drawdown limit from 120 per cent to 150 per cent to allow more flexibility to those who would otherwise buy an annuity
- increase the size of a single pension pot that can be taken as a lump sum, from £2,000 to £10,000

¹⁸⁶ Finance Act 1995, Schedule 11 Personal Pensions: Income Withdrawals

¹⁸⁷ HM Treasury, Removing the requirement to annuitise by age 75, July 2010 p 7, para 2.5

¹⁸⁸ HM Treasury, Removing the requirement to annuitise by age 75, July 2010, p 7, para 2.6

¹⁸⁹ HM Treasury, Removing the requirement to annuitise by age 75: A summary of the consultation responses and the Government's response, December 2010, pp 7-14

- increase the number of pension pots of below £10,000 that can be taken as a lump sum, from 2 to 3
- increase the overall size of pension savings that can be taken as a lump sum, from £18,000 to £30,000.¹⁹⁰

The Chancellor said in his Budget speech that “these measures alone would amount to a radical change.”¹⁹¹

110. Otto Thoresen, Director-General of the Association of British Insurers, shared the Chancellor’s view. He described the immediate changes as “a big challenge for the industry and for the individual consumers affected”.¹⁹² In particular, he identified the speed at which the changes needed to be made as a challenge for providers, saying that “When you begin to make these changes to draw-down limits and the rest, the technology and systems implications of those changes are not insignificant”.¹⁹³ He did, however, consider this challenge to be “manageable”.¹⁹⁴

111. The ABI’s briefing on the Budget said that these changes would have “an immediate impact on customers who may be in the middle of purchasing an annuity.”¹⁹⁵ Mr Thoresen told us that the industry’s response to the immediate changes announced in the Budget had been “to extend cooling-off periods.”¹⁹⁶ He added:

[W]e have had to work in partnership with HMRC, because there are tax implications of unwinding these types of transactions. HMRC has been working hard since the Budget to clarify the many and various different situations that occur.¹⁹⁷

112. On 27 March 2014, the Government stated that:

[...] people who have recently taken a tax-free lump sum from their defined contribution pension will be given more time to decide what they wish to do with the rest of their retirement savings and will not be put at a disadvantage should they wish to wait to access their pension savings more flexibly.¹⁹⁸

In the light of this, HMRC issued guidance on 9 April 2014. It explained that it had:

[...] provided more information to help people who want to use the new flexibility. This information is for people who have:

190 HM Treasury, Budget 2014, 19 March 2014, p44, para 1.164

191 HC Deb (2013-14), 19 March 2014, col 793

192 Q467

193 Q471

194 Q471

195 ABI, Budget briefing, 24 March 2014

196 Q467

197 Q469

198 www.gov.uk, News story: Pensions freedom for 400,000 hardworking people from today (HM Treasury), Published 27 March 2014

- received a tax-free lump sum on or before 27 March 2014
- either cancelled an annuity contract within the cooling-off period on or after Budget day (19 March 2014) that was linked to that lump sum or not yet decided how to access the rest of their pension savings.¹⁹⁹

On the same day, the FCA issued guidance to financial firms on how they would expect firms to handle the immediate changes. The FCA explained that:

In light of these policy announcements, firms will need to make changes to their operational processes and procedures. They will also need to consider how to treat those customers who are making decisions about their retirement income in this interim period. We are issuing guidance to outline our expectations of firms during this interim period.²⁰⁰

Pension reforms from April 2015

113. The Budget announced a package of changes to pension taxation that would take effect from April 2015. It described these reforms as “radical changes that will offer people more options in how and when they access their defined contribution pension.”²⁰¹ Alongside the Budget, the Government published a consultation paper *Freedom and choice in pensions*, which set out the proposed reforms:

- Removing the 55 per cent tax charge for full withdrawals from defined contribution pension savings
- Treating any amount of income drawn from pension savings after the age of 55 as income and therefore subject to marginal rate of tax.
- Removing the minimum income requirement for flexible drawdown
- Removing the drawdown limit and review requirements associated with capped drawdown thereby bringing this type of income drawdown to an end.²⁰²

114. In addition, the Government announced that it would introduce a “guidance guarantee”,²⁰³ under which “all individuals with a defined contribution pension in the UK approaching retirement will be offered guidance at the point of retirement that:

- is impartial and of consistently good quality
- covers the individual’s range of options to help them make sound financial decisions and equip them to take action, whether it is seeking further advice or purchasing a product

199 HMRC, [Budget changes - pension flexibility and changes to Finance Bill 2014](#), 9 April 2014

200 Financial Conduct Authority, [FG14/3 Guidance, Budget 2014 - Pension reforms: guidance for firms in the interim period](#), April 2014

201 HM Treasury, Budget 2014, p42, para 1.157

202 HM Treasury, [Freedom and choice in pensions](#), pp 19-21

203 HM Treasury, *Freedom and choice in pensions*, p31, para 4.12

- is free to the consumer
- is offered face to face.”²⁰⁴

115. These changes apply to defined contribution pensions. Members of public defined benefit schemes will not be permitted to transfer to a defined contribution scheme to take advantage of these reforms as, in the Government’s view, this would “be unfair on both the taxpayer and remaining scheme members”.²⁰⁵ The Government is consulting on the circumstances in which members of private defined benefit schemes might be allowed to transfer. The Government is concerned that “large scale transfer (or anticipated transfer) of members of private sector defined benefit schemes to defined contribution schemes could have a detrimental impact on the wider economy”.²⁰⁶

The importance of choice

116. The Government’s pension reforms emphasise the importance of consumer choice. This was welcomed by many of those who gave evidence to our inquiry. Otto Thoresen, Director-General of the Association of British Insurers (ABI), described the increase in choice for consumers as “positive”.²⁰⁷ He also told us that the changes announced in the Budget created “the opportunity for a far more effective market for people retiring”.²⁰⁸ Chris Woolard of the FCA said that:

The fact that there are now more choices potentially on the table for consumers at the point at which they either decide to purchase an annuity or do something different, we would be welcoming those changes.²⁰⁹

Chris Hannant, Director-General of the Association of Professional Financial Advisers (APFA), said that he thought that “people should have control of their money”. He added: “I think you do not stumble into a substantial pension pot by accident and you should be rewarded for taking the responsibility to save”.²¹⁰ For his part, Robin Fieth, Chief Executive of the Building Societies Association, said that “the concept of allowing people to have responsibility for their own money makes a lot of sense.”²¹¹ The IFS identified the advantages of the liberalisation announced in the Budget:

It will allow people freedom to manage, and make choices over, their own affairs. It will likely increase the incentive to save in a pension.²¹²

117. We asked Jane Vass, Head of Public Policy, Age UK, whether people could be trusted with their own money. She told us:

204 HM Treasury, Freedom and choice in pensions, pp30-31, para 4.11

205 HM Treasury, Freedom and choice in pensions, p 34, para 5.6

206 HM Treasury, Freedom and choice in pensions, p 34, para 5.12

207 Q471

208 Q452

209 Q243

210 Q300

211 Q300

212 Institute of Fiscal Studies, IFS Budget Analysis: introductory remarks, 20 March 2014, p 7

I think people are generally very sensible. They are the ones that lose out if they do not take care with their money and I think people will generally make good decisions.²¹³

Dr Ros Altmann, a pensions expert, told the Committee:

[...] this revolutionises the way pensions as a whole can work, both on the accumulation phase and on what I think will be a more flexible and gradual withdrawal, importantly leaving some extra money for social care that people are going to need but currently have not made any provision for.²¹⁴

Joanne Segars, Chief Executive of the National Association of Pension Funds (NAPF), welcomed the changes but cautioned that “that there needs to be the right protections in place and the right support in place to help people make the expanded range of choices they have.”²¹⁵

118. The Committee notes that all witnesses welcomed the greater flexibility and choice provided by the Government’s proposed pension reforms. We further note the Chancellor’s commitment to “free, impartial, face-to-face advice”, which will be important for many people for the reforms to work.

The responsibility of choice

Auto-enrolment

119. We considered whether the increased choice for consumers at retirement was consistent with the Government’s auto-enrolment policy. Auto-enrolment will ensure that every qualifying worker will have to be enrolled onto a workplace pension, and that both they and their employer will make contributions unless the employee actively opts-out.²¹⁶ The NAPF described the proposed pension reforms as “perplexing” when compared to the principles and assumptions that underlie auto-enrolment:

Given that we have introduced auto-enrolment because people do find it very difficult to make these decisions, we have then said at the end people can have that freedom.²¹⁷

120. The principle of freedom at retirement is not necessarily incompatible with the idea that people should be actively encouraged to save into a pension in the first place. Gemma Tetlow, of the IFS, said:

There are perhaps two potential reasons for auto-enrolment. One would be that people are very short-sighted. Therefore, even if it is quite easy for them to make the

213 Q279

214 Q274

215 Q299

216 HM Government, [Workplace pensions](#), accessed: 9 April 2014

217 Q296

choice to opt into a pension, they do not see the benefit of it because they discount the future.

The second perhaps would be that it is quite a lot of hassle to get yourself organised with a pension. If the default is that you are making those contributions, it removes that hassle factor from you. To get rid of the requirement to buy an annuity later on, I think you would have to believe that people are somewhat less short-sighted at the age of 55 or certainly less short-sighted about the end of their lives at that point.²¹⁸

121. Otto Thoresen did not, however, see any tension between auto-enrolment and the Government's pension reforms:

I don't, actually. I have always felt, even before the events of the last four weeks, that the concept of auto enrolment and the nudge philosophy was fine when you were trying to get people started on a savings habit. Making it easy for them to continue with that savings habit is very sensible. But there was always going to be a point in the process where the individual had to start to understand that they were building up the assets on which they were going to have to live when they were no longer earning money through work, and they were going to have to then start to think about their own personal situation: about the state of their mortgage; their indebtedness; their ability to go on working in retirement; whether they had dependants; and whether they had elderly dependants. There is a long list of factors you have to start taking into account, which reflect the fact that you have stopped being one of many who all broadly have the same savings need to being a whole lot of individuals who each have a different set of challenges to deal with when you arrive at a retirement decision. So that process of transition from inertia to ownership and personal responsibility was something we were going to have to face up to, anyway. What this has done, though, is to raise the questions that would have come with that transition earlier. That is where I think the challenge is over the next 12 months.²¹⁹

The Chancellor agreed that there was no contradiction between auto-enrolment and pension liberalisation:

We want to see more savings. One of the very encouraging things about auto-enrolment is that 3 million more people now have pensions. The projections are that that will increase substantially. I think you make pension saving more attractive when you give people greater freedom.²²⁰

The uncertain impact of the reforms

122. It is too early to tell how consumers will exercise the new freedoms given to them by these reforms. The OBR said that the impact of the reforms on the public finances was "particularly uncertain".²²¹ We asked its Chairman Robert Chote whether the ability to take

218 Q69

219 Q481

220 Q412

221 HM Government, Budget 2014: policy costings, p 66, para B.8

pensions as a lump sum might raise household consumption and lower the savings ratio. He told us:

We are assuming that, if you look at the set of pension and saving measures in total, there are effects going in both directions and, therefore, we have not made an explicit adjustment to the forecast for that. That is not because we are very confident that the answer is zero. It is because there are things going in both directions and we do not think we can be clear which way wins out.²²²

The assessment of the IFS was that:

The liberalisation of pension rules is expected to lead to more tax revenue over the next few years. But that depends on highly uncertain behavioural assumptions about when people take the money.²²³

The FCA told us that it would use its Market Study to reach its own conclusions about the likely impact on the market.²²⁴ The Chancellor himself acknowledged that the effects of the reforms were difficult to predict, saying:

Let me be clear, it is a new area of policy. This is uncertain. We will see what happens.²²⁵

123. With increased consumer choice comes an increased burden of responsibility on consumers. Joanne Segars of the National Association of Pension Funds told us that the reforms “clearly expand the range of choices that people have, but we have also been very clear that with that choice comes responsibility”.²²⁶ Otto Thoresen of the ABI told us:

The consequence of giving people choice and freedom to use their retirement assets in the way they choose is that they will make decisions and we will have to live with the consequences.²²⁷

124. Until consumers begin to use this overhauled market we cannot know what the impact of these reforms will be. The extension of consumer choice brings with it a number of uncertainties and risks. We examine these further in this chapter.

Falling back on to the welfare state

125. In his speech on the Budget, the Chancellor said that the pension reforms announced in the Budget were only possible because:

[W]e have a triple lock on the state pension; more people are saving through auto-enrolment; and we are introducing a single-tier pension that will lift most people

222 Q204

223 Institute of Fiscal Studies, IFS Budget Analysis: introductory remarks, 20 March 2014, p 3

224 Q245

225 Q410

226 Q298

227 Q475

above the means test. That secure basic income for pensioners means that we can make far-reaching changes to the tax regime to reward those who save.²²⁸

The Minister of State for Pensions, Steve Webb MP, identified the single-tier state pension as a crucial element in facilitating the reforms, saying:

In the past, Governments were concerned that if people had freedom over their pension pots, they would run them down too quickly and then depend on state support in later life. The single-tier pension provides a game-changing opportunity to rethink this model. With people receiving a full single-tier pension already clear of the basic means test, the state need be much less prescriptive about how people use their accumulated pension savings.²²⁹

The single-tier state pension will be introduced from 6 April 2016.²³⁰ The reforms will:

Restructure current expenditure on the state pension into a simple flat-rate amount, to provide clarity and confidence to better support saving for retirement. Those already over State Pension age when the reforms are implemented will continue to receive their state pension (and the Savings Credit, where applicable) in line with existing rules.²³¹

126. One of the risks of the pension reforms announced in the Budget is that pensioners will exhaust their pension pot too early and need to fall back onto the safety net of the welfare state as a result. Dr Ros Altmann considered that that the reforms to the state pension reduced the risks to the public purse, but had not eliminated them entirely. She told us:

I do think that people who have saved in a pension would typically not be the ones that will fall back on the state, but there is that risk. I accept that. I think the new single-tier state pension will be very helpful and it was an important part of the picture to try to reform the state pension system to have one that hangs together whereby it is safe to save. We still have the problem of council tax benefit and housing benefit. I do accept that, but at least the issue is less than it was before.²³²

Gemma Tetlow, of the Institute for Fiscal Studies, agreed that the risk was reduced but not eliminated:

Virtually everyone will qualify for a single-tier pension that will be slightly above the level of pension credit. That does mean it slightly reduces the number of people who would be expected to end up on means-tested benefits in retirement relative to the

228 HC Deb (2013-14), 19 March 2014, col 792

229 HC Deb (2013-14), 20 March 2014, col 951

230 Department for Work and Pensions, [Government confirms 2016 start for new flat rate State Pension](#), Accessed 9 April 2014

231 Department for Work and Pensions, *The single-tier pension: a simple foundation for saving*, p 8, para 13

232 Q294

current system. However, it does not mean that no one is likely to end up on means-tested benefits.²³³

She confirmed that there was a risk of additional future costs to the Treasury and that there remained a taxpayer interest in the impact of the reforms.²³⁴ She said:

Importantly, pension credit is not the only means-tested benefit that many pensioners qualify for. A lot also qualify for housing benefit and council tax benefit, which continue much further up the income distribution than pension credit does. The Department for Work and Pensions, for example, in their impact assessment for the single tier reforms, estimated that by 2060 under the single tier system about 15% of pensioners would still be eligible for some form of means-tested benefit and that excludes council tax support.²³⁵

127. We asked the OBR whether it had made any assessment of the likelihood that the pension reforms could have a detrimental impact on the public finances—for example, in the form of increased social care bills or increased housing benefit needs. Robert Chote told us that they had not made such an assessment, “partly because of the relatively short time horizon over which we look for these sorts of forecasts.”²³⁶ He added:

I think it is a question that we will probably want to return to in the longer-term fiscal sustainability report, as to whether that is something we want to make any sort of an adjustment for, but I think the chances of much of that showing up as a serious pressure within a five-year horizon are relatively modest.²³⁷

128. Joanne Segars, Chief Executive of the NAPF, thought that the risk of pensioners exhausting their savings and needing to fall back on the state was limited. She told us:

Evidence does suggest and, if we look at Australia, we do see that there the people are not blowing it all in one go. Clearly it is not possible to make exactly like-for-like comparisons, but we do see that financial responsibility grows with age but also as people’s pension pots grow.²³⁸

129. The Government is currently undertaking a significant reform of the way in which long-term social care is funded. The reforms include a new means test threshold of £123,000 for government-funded long-term care. These reforms will come into force at the same time as the pension reforms in April 2015.²³⁹ The interaction between increased choice in how to use pension savings and the reformed long-term care model is of great importance to the welfare of retirees and to the public finances. It is not yet clear how the two sets of reforms will interact. On the one hand, it may be that the pension reforms will

233 Q65

234 Q66

235 Q65

236 Q210

237 Q210

238 Q317

239 Department of Health, [Landmark reform to help elderly with care costs](#), 11 February 2013, Accessed 9 April 2014

assist pensioners in planning for their long-term social care needs. Dr Ros Altmann told us that she expected to see:

[...] a more flexible and gradual withdrawal, importantly leaving some extra money for social care that people are going to need but currently have not made any provision for.²⁴⁰

On the other hand, the pension reforms might tempt people to exhaust their pension pot to avoid being liable for the costs of their own long-term social care. Many savers may be unaware of the interaction between the pensions system and the social care means test. Joanne Segars of the National Association of Pension Funds explained:

If you end up taking the money as one lump sum, that could count against you if you need social care benefits.²⁴¹

Age UK pointed out that the means test for care allows local authorities to take into account undrawn pensions. It warned:

Many people will be unaware of this, and it is unclear how the notional value of the pension would be calculated under the new regime. The impact of the 'deprivation of assets' rules if people withdraw savings for purposes which could be deemed inessential is also unclear.²⁴²

130. We asked witnesses from the OBR whether they considered it their responsibility to recommend that the Government reassess the overall cost of long-term care in light of changes in the behaviour of pensioners. Robert Chote said that that was not the role of the OBR, but added:

What we want to do is to see what a sensible long-term projection of social care costs was. To date, we have done that very much looking on an assumption that is based around demographics rather than this sort of influence. I do not know whether, when we looked at it, we would think that was something that we could bring a particularly informed additional view to, but we will have a look at it.²⁴³

131. The Chancellor said that, following these pension reforms, the means test for social care would need to be revised:

The current social care means test does not take into account [...] the changes to the flexibilities around pensions and so we need to change the social care means test to take that into account. I am absolutely clear that we want to make sure that this does not have an impact.²⁴⁴

132. The full impact of the pension reforms on the long-term social care budget remains uncertain. The Government is right to require the long-term care means test to

240 Q274

241 Q318

242 Age UK, [written evidence](#)

243 Q211

244 Q390

be revised in the light of these reforms. The Government has an understandable desire to have the radical changes to pensions completed as soon as possible. Because the reforms both to pensions and to long-term care come into force simultaneously, the revision of the long-term care means test should be completed in time for those who may be affected by both these reforms to make informed choices.

Longevity risk

133. The Government's consultation paper says that "Over the past few decades retirement has changed significantly".²⁴⁵ The paper identifies increased life expectancy as one of the major causes of this change. It notes that:

When the basic State Pension was introduced in 1948, a man reaching age 65 could expect to live for only 12 years, and a woman for 15 years. People are now living far longer. A man reaching age 65 in 2012 can now expect to live for 21 years, and a woman for 24 years.²⁴⁶

134. People can expect to live longer retirement, so they may have a period of retirement in which they are relatively active and then a period in which they have complex health and care needs. This may mean that alternatives to the universal single-life annuity product might be more suitable for some people. As Dr Ros Altmann explained:

The annuity will cover against one risk. It is like buying a house and insuring against fire. The annuity will cover you against the risk of living a very long time, but there are many other risks in retirement that people face that certainly a standard annuity will not cover you for. It is like having fire insurance but then you get flooded or burgled and you do not have any cover. The standard annuity will not cover you against inflation or for a partner.

This was one of the problems. The annuity market has been regulated as if annuities are a no-risk product suitable for everybody and that simply is not the case.²⁴⁷

135. Following the reforms announced in the Budget, those who do not purchase an annuity will need to manage their finances to meet their own needs. This includes managing the risk that they might live for longer than they expect. When asked how well consumers were able to estimate their own longevity, David Geale of the FCA told us:

It is something very difficult and it is a very difficult question to even ask yourself: how long am I going to live? It is an answer that people perhaps underestimate, particularly when you build in the interaction of things like long-term care. Even if we make a reasonable assumption of how long we might live, we may not allow for the fact that we may need care provided over that period.²⁴⁸

245 HM Treasury, Freedom and choice in pensions, March 2014, para 2.1

246 HM Treasury, Freedom and choice in pensions, March 2014, p 9, para 2.2

247 Q272

248 Q266

Joanne Segars of the NAPF told us that there was evidence that people generally underestimated their own longevity. She said:

We know that people under-estimate how long they are going to live, women by four years on average and men by two years. We know that people under-estimate exactly how much they have in their pension pot and what exactly that will buy them and there are some quite complex issues to consider.²⁴⁹

The Institute for Fiscal Studies pointed out that:

Even if individuals have thought carefully about their retirement and think they have accumulated sufficient resources to fund it, this may not actually be the case. While DB schemes insure their members against the risk of living ‘too long’ from the point at which they first join the scheme, DC scheme members do not get this insurance until they purchase an annuity.²⁵⁰

136. Until now there have been very strong incentives to purchase an annuity at the point of retirement. Creating greater freedom and choice in retirement will require individual consumers to consider the range of circumstances they may face, in particular relating to longevity. They will need to make informed decisions based on their personal needs and likely circumstances. For some consumers, these choices will require substantial guidance.

Financial innovation

137. Creating a tax environment which supports innovation within the retirement market is a crucial feature of the proposed pension reforms. In its consultation document, the Government says that it expects the reforms:

[...] to stimulate innovation and new competition in the retirement income market, with providers creating new products to satisfy individual consumer needs and meet new social challenges such as funding care later in life [...]. It will also expand the market to allow further development of existing products, such as deferred annuities.²⁵¹

138. David Geale from the FCA thought that it was “too early to tell” how the market might respond to the changes, but considered that there was the “potential [...] for product innovation”.²⁵² Joanne Segars, of the NAPF, also saw this potential. She told us:

What we would hope to see is more innovation in this market with products being developed that lead into long-term care products, for example, that are much more flexible and perhaps more accurately match the spending patterns that people face in

249 Q318

250 Institute of Fiscal Studies, Expectations and experience of retirement in Defined Contribution pensions: a study of older people in England, November 2012, p 11

251 HM Treasury, Freedom and choice in pensions, p 23, para 3.19

252 Q250

retirement. I think there is potential here for more innovation and then it is for those pension providers [...] to meet that new demand, to rise to that challenge.²⁵³

Chris Hannant, of APFA, expected to see “a market that generates products that are better tailored to the needs of the consumer”.²⁵⁴

139. The financial sector’s past performance in meeting consumer need through innovation was criticised by the Parliamentary Commission on Banking Standards, which found that:

Banks have incentives to take advantage of these customers by adding layers of complexity to products. A good deal of the innovation in the banking industry makes products and pricing structures more complex, hindering the ability of consumers to understand and compare the different products.²⁵⁵

Demand and capacity to supply

140. As we have already noted, flexibility in pensions has increased over time. Nevertheless, those who choose to make use of this flexibility by drawing down their income are still in the minority. At present, sixteen times more funds enter annuities than income drawdown.²⁵⁶ Now that pension flexibility is to be increased still further, a greater range of consumers will want to make use of that flexibility. As Otto Thoresen of the ABI told us:

There are about 400,000 people retiring through this process every year. The vast majority of those, 60% of those, have small pots—the amounts involved are £30,000 or less. The fact is that for many of those individuals what is being created here is an environment in which they have far more choice.²⁵⁷

141. A wide range of annuity products are now available. Enhanced annuities sold as a proportion of all annuities has increased from 7 per cent to 24 per cent in 5 years²⁵⁸. Investment-linked annuities and escalating annuities, however, each constitute less than 5 per cent of the market.²⁵⁹ It may be that the demand for new innovative retirement products will be for income drawdown products rather than annuities. As Dr Ros Altmann describes:

When companies realise that there is a market or will be a market for products that have not yet existed. I do not know how long that will take but I certainly know that there are companies now working on ways of developing a kind of pension income type product. Drawdown and flexible drawdown, as they currently exist, are very expensive. The fees associated with those have resulted in them being unsuitable for

253 Q311

254 Q312

255 Parliamentary Commission on Banking Standards, *Changing banking for good*, Volume I, p 19, para 23

256 Financial Conduct Authority, *Thematic review of annuities*, February 2014, p 5

257 Q471

258 Association of British Insurers, *The UK Annuity Market: Facts and Figures*, February 2014

259 Financial Conduct Authority, *Thematic review of annuities*, February 2014, p 9

small pension funds and very costly for any size pension fund, partly because of the restrictions that were on them and partly because of the way the market worked there was not a lot of competition anyway.²⁶⁰

Otto Thoresen described how he saw the market developing:

I believe that the model that we will move to will be something that looks like cash for people with relatively small pots; and in the middle territory, an option that allows you to move into quite a simple and more balanced investment vehicle—call it draw-down, for the sake of no other label being available at the moment—which allows you to stay invested but still take income, and at a point when you are older, where you want the certainty that an annuity provides and the price of the guarantee is no longer as onerous, then you move into an annuitised position.²⁶¹

Potential for mis-selling

142. The reputation of the financial industry has been damaged by considerable large scale mis-selling, with payment protection insurance being the most recognised example. The 1990s saw the mis-selling of personal pensions and free standing additional voluntary contributions.²⁶² We asked Otto Thoresen, Director-General of the Association of British Insurers, whether there might be a danger that pensions would be mis-sold, or poor advice given to consumers, as firms adjusted to the new arrangements. He told us:

Because there will be more people making those decisions than there would have been otherwise, to say that there is no increase in risk would be an overstatement. But I do not see it as the most significant issue we have to deal with.²⁶³

143. For her part, Jane Vass of Age UK considered that it was the regulator's responsibility to guard against this risk:

The onus should not be on the individual but on the industry and the regulators to ensure that products that come up are sensible. That will mean a much more interventionist approach than in the past.²⁶⁴

The Parliamentary Commission on Banking Standards made the following recommendation on early intervention by the regulator:

The FCA has powerful new tools to intervene in products. [...] Their use by the FCA will carry significant risks. How the FCA's new product intervention tools are used will be a key indicator of its success in taking a judgement-led approach. The balance between intervening too early, distorting the market, and too late, potentially

260 Q273

261 Q474

262 The Pension Advisory Service, [Pension mis-selling](#), accessed: 10 April 2014

263 Q473

264 Q280

allowing customers to suffer, will be a delicate one, and how these tools are used will be an indicator of the FCA's success in taking a judgement-based approach.²⁶⁵

This recommendation is as relevant to the pensions and insurance industries as it is to the banking sector.

144. The market is likely to adapt, offering a new range of financial products for those approaching retirement. It is crucial that these products are not defective. Were they to be so, the reputation of the financial services industry, which has suffered severe damage in recent years from large scale mis-selling, would be further tarnished.

145. The FCA has now been given new powers to intervene early, in advance of detriment occurring. In practice, this will be extremely difficult to accomplish without creating other forms of consumer detriment. In particular, it will be essential to avoid stifling market innovation. The use of these new powers will be a major test of judgement-based regulation.

The future of the annuity market

146. In 2013 the annuity market was worth £11.9 billion in total, with 353,000 annuities sold.²⁶⁶ As larger defined contribution savings mature in 2012 the individual annuity market was expected to grow in the short-term to £23 billion by 2014–15.²⁶⁷ In his Budget speech the Chancellor said “no one will have to buy an annuity”.²⁶⁸ After his speech, the share prices of a number of annuity providers fell, with “close to £3bn wiped off the value of listed firms”.²⁶⁹

147. A central justification of the Government's proposals is that the annuity market is not working for consumers. As the Chancellor wrote in his Foreword to the reforms:

The annuities market is currently not working in the best interests of all consumers. It is neither competitive nor innovative and some consumers are getting a poor deal. It is time for a bold, modern and progressive reform.²⁷⁰

The FCA's recent thematic review found that that 97 per cent of the market for open market standard annuity sales was held by just three providers.²⁷¹ David Geale, of the FCA, told us that “the thematic work has given us the conclusive evidence that the market is not working well for consumers and made the case for change”.²⁷² Other witnesses also criticised the current performance of the annuity market. Dr Ros Altmann said of the FCA's study:

265 Parliamentary Commission on Banking Standards, *Changing banking for good*, Volume I, p58, para 186

266 Association of British Insurers, *The UK Annuity Market: Facts and Figures*, February 2014, p 1

267 Pension Institute and National Association of Pension Funds, *Treating DC scheme members fairly in retirement?*, February 2012, p26

268 HC Deb (2013-14), 19 March 2014, col 793

269 *Financial Times*, Budget 2014: Insurers lose £3bn after pension fund shake-up, 19 March 2014

270 HM Treasury, *Freedom and choice in pensions*, March 2014, p 3

271 Financial Conduct Authority, *Thematic review of annuities*, p 20

272 Q232

I must confess that for people who have looked at the market, studied it and understood it in detail for a long time, it certainly did not reveal anything new. There is plenty more that could have been uncovered or investigated that I hope will still be so as the regulator gets to grips with what I believe is one of the most significant regulatory failures that we have seen in the financial system.²⁷³

Jane Vass, of Age UK, said that:

Our concern has been well noted around the lower value end of the market, where we have been calling for liberalisation for some time. It has been a concentrated area. Rates have not been as good and we have been calling for a wider review of the whole decumulation area.²⁷⁴

Joanne Segars, of the NAPF, also agreed that the market was dysfunctional and said that:

We produced a report two years ago now that showed that about £1 billion a year leaks out of the annuities market because people do make poor decisions or they do not get the right annuity for them.²⁷⁵

148. Following the Budget, market analysts produced a range of projections of the future size of the individual annuity market. RBC Capital Markets estimated the market would contract by 90 percent,²⁷⁶ Barclays Equity Research said the market “could decline by two-thirds from £12bn to £4bn per annum within the next 18 months”,²⁷⁷ and Legal and General’s Chief Executive Nigel Wilson estimated that the market would shrink by £2.8 billion a year with an overall decline by up to 75 percent.²⁷⁸

149. None of the evidence we received disagreed that these reforms would change the market, but as Joanne Segars of the NAPF pointed out to us, the effect of these reforms on the annuities market is not easy to predict. She said “the big unknown in all of this, of course, is how much demand there will still be for annuities in whatever form going forward”.²⁷⁹ Chris Woolard of the Financial Conduct Authority told us that predictions that the annuities market would effectively disappear due to the changes might be too pessimistic. He said:

If you look at the experience of other countries, despite predictions there of markets sometimes disappearing on the back of certain changes, I think the case has often been that that is not what has happened. Switzerland is a very different regulatory environment. We ought to be careful about stretching the analogy too far, but if you look at Switzerland, they have gone through a very similar deregulation and still 80%

273 Q269

274 Q270

275 Q297

276 “Budget 2014: Pensions revolution casts pall on insurers”, *Financial Times*, 20 March 2014

277 “Budget 2014: Pensions shakeup could kill off annuity market, say analysts”, *The Guardian*, 20 March 2014

278 “L&G sees UK individual annuity market shrinking 75 percent”, *Reuters*, 26 March 2014

279 Q312

of people who are retiring choose to buy an annuity there. I think we have to be very careful about predictions of doom.²⁸⁰

For his part, Otto Thoresen of the ABI expected that initial market contraction would be followed by recovery:

In the next five to 10 years [you will see] lower levels of annuity take-up, but as people move through their retirement process, a recovery and growth again in the annuity market, because its positive aspects continue to be positive—the certainty it gives people and their ability to plan for the future, and they know that they will not run out of money.²⁸¹

150. We considered the possibility that a reduced pool of annuitants might lead to poorer rates and further reduced demand for annuities. Dr Ros Altmann thought that this was unlikely:

From the pricing perspective of annuities, certainly all the analysis that I have done, [...] suggests that certainly the average annuity and the annuity that most people would have been buying that they had been rolled into from their existing pension provider now represents such poor value it is difficult to imagine the value worsening. [...] It is difficult to see a case for standard annuities to become more expensive, so I would not be concerned that they do.²⁸²

Otto Thoresen, on the other hand, suggested that rates might continue to worsen under certain circumstances:

A number of factors could lead to rates being poorer, but I do not think it is contraction in the market so much. We are already on a path that was leading to a different annuity market, anyway. The advent of the enhanced annuity providers who effectively underwrite the client at the point of their taking their annuity meant that you were beginning to get a healthier pool of customers in the standard annuity market. If you have a healthier pool of customers, they will live longer. If they live longer, clearly the rate that the market as a whole can offer will become less attractive. One factor certainly could apply: if the only people who take annuities are a particular type of individual that will shape the annuity pool and the pricing. But I do not think contraction in itself is likely to be the issue.²⁸³

He also highlighted the fact that current prudential rules mean that those who annuitise early lead to a greater capital cost to the insurer. He was optimistic that these reforms could reduce that cost and thereby improve the market:

One of the challenges of writing annuity business is that you are offering effectively a 30-year guarantee. The Prudential regulator, not surprisingly, wants you to hold solvency capital to support that [...]. If we can move to a point where people

280 Q246

281 Q474

282 Q274

283 Q479

annuitise at the right time, you could see an improvement in the way the market operates.²⁸⁴

151. In its consultation, the Government stated that “those who continue to want the security of an annuity will be able to purchase one, either at the point of retirement, or at a later stage”.²⁸⁵ The Chancellor told us that:

It is important to say that annuities would be the right product for many people after these reforms. They are not the right product for everyone. Some people want the certainty that annuities can provide.²⁸⁶

The FCA also said that annuities remained a suitable product for certain consumers.²⁸⁷ Joanne Segars agreed, saying:

Fundamentally there are large number of people who, in retirement, want a regular income. They want that certainty of a regular income with some inflation-linking perhaps, with the ability to leave something to their spouse or partner. When you ask people what they want, lots of people say, “What I want is a regular income for the rest of my life and I can leave something to my spouse”.²⁸⁸

152. The impact of these reforms on the annuity market will only be known after a number of years. Increased flexibility and choice in retirement will only benefit consumers if an active and innovative market offers a range of products, which should include annuities, to suit individual requirements.

The guidance guarantee

153. The Government’s consultation paper welcomes “the recent statement by the Association of British Insurers (ABI) committing pension providers to provide, at the point of retirement, ‘a conversation for customers with their pension provider or an impartial advice or guidance service about their retirement options.’”²⁸⁹ It describes this commitment as “an important step forward in improving the guidance that consumers want and need.”²⁹⁰ The Government proposes to legislate on a “right to financial guidance” for people at retirement.

154. Building on previous work, the ABI made a commitment that, by summer 2015, its members would provide:

A conversation for customers with their pension provider or an impartial advice or guidance service about their retirement options. This conversation will include a high-level overview of alternatives to annuities as people approach retirement.

284 Q479

285 HM Treasury, Freedom and choice in pensions, p 20, para 3.14

286 Q407

287 Q246

288 Q313

289 HM Treasury, Freedom and choice in pensions, p 30, para 4.10

290 HM Treasury, Freedom and choice in pensions, p 30, para 4.10

A comparison of annuity quotes for customers, whereby all providers will offer a comparison, or introduction to an intermediary who will deliver the comparison, early and prominently in their retirement process. The comparison will be offered as an integral part of the process not as an optional extra.

Ask all customers for information about their health and lifestyle, which they can use to shop around for an enhanced rate.²⁹¹

155. The Chancellor told us that he did not think “people are getting [...] particularly good guidance at the moment”.²⁹² The Government proposes that all individuals with a defined contribution pension be offered guidance that is:

- impartial and of consistently good quality
- covers the individual’s range of options to help them make sound decisions and equip them to take action, whether that is seeking further advice or purchasing a product
- free to the consumer
- offered face to face.²⁹³

156. This guidance will be crucial to ensuring that consumers are empowered to make the best possible use of the flexibility offered by the Government’s reforms, given the imbalance of information between many of the buyers and sellers of financial products, and the complexity of decisions which relate to tax liabilities, care costs and interaction with certain Government means-tested benefits. Joanne Segars emphasised the complexity of the retirement choices that consumers have to make:

It is the interaction with a much wider set of issues than just purchaser and seller. It is the interaction with the tax system and the interaction with the social care system.²⁹⁴

Guidance also helps to ensure that consumers are not only better placed to avoid mis-selling but also to contribute to creating discipline within the market through competition. As the Parliamentary Commission on Banking Standards found:

Empowering consumers to make better decisions about the merits of banking services is not simply a means of avoiding future scandals. Informed consumers are better placed to exert market discipline on banks more generally and, in doing so, encourage banks to compete on price and service.²⁹⁵

157. We set out below the key issues that the Government and the FCA should address in developing the guidance guarantee and the standards which will underpin it.

291 Association of British Insurers, ABI sets out reforms to help boost retirement incomes for millions of savers, 10 March 2014

292 Q423

293 HM Treasury, Freedom and choice in pensions, March 2014, pp 30-31

294 Q319

295 Parliamentary Commission on Banking Standards, Changing banking for good, Volume II, June 2013, p 241, para 407

Guidance, advice and consumer protection

158. In his Budget speech the Chancellor described the ‘guidance guarantee’ as:

A new guarantee, enforced by law, that everyone who retires on these defined contribution schemes will be offered free, impartial, face-to-face advice on how to get the most from the choices they will now have. [Emphasis added]²⁹⁶

On the other hand, the Government’s consultation paper said that the Government would introduce:

a new guarantee that all individuals with a defined contribution pension in the UK approaching retirement will be offered guidance at the point of retirement. [Emphasis added]²⁹⁷

When we asked the Chancellor about this, he described the difference between advice and guidance as “a technical distinction”, and said that his Budget speech needed “to communicate in English so that people watching it can understand what is meant”. He added:

The issue that you have raised was not something that the consumer groups have had a problem with. They have all understood what exactly was meant. I think the general public have understood what was meant as well, which is the purpose of the Budget speech.

159. The distinction between ‘advice’ and ‘guidance’ may be a technical one, but it is nevertheless important. Chris Woolard, of the FCA, told us:

Advice, with a capital A, and guidance are absolutely not the same thing in terms of how we approach the rulebook for the industry. Advice, in terms of regulated advice, carries with it a series of guarantees and protections that are provided around it.²⁹⁸

Dr Ros Altmann said the word advice was “a problem”,²⁹⁹ while Joanne Segars, of the NAPF, said that “consumers tend to confuse ‘Guidance’ and ‘Advice’”.³⁰⁰ The FCA added that:

Within our rulebook full-blown regulated advice is pretty well understood by both firms and consumers when they go and get it. It feels like a very formal process. Similarly, so-called execution only, where you decide to do something completely yourself, is pretty well understood by people. The piece in the middle is often quite murky for the firms themselves sometimes but definitely for consumers.³⁰¹

296 HC Deb (2013-14), 19 March 2014, col 793

297 HM Treasury, Freedom and choice in pensions, March 2014, p 30, para 4.11

298 Q257

299 Q281

300 Q335

301 Q267

160. The FCA acknowledged that there was a clear difference in liability for consumers who decide to purchase a financial product after having received “advice” and those who do so having received “guidance”. In the case of guidance, Chris Woolard told us:

The responsibility rests with the consumer and the risks around making a decision rest with the consumer in a guidance situation.³⁰²

The implication of this is that consumers who receive guidance will have no recourse to the Financial Ombudsman Service. The providers of the guidance would only be liable:

[...] if the firm or whoever is providing that guidance has misled somebody, but it would not be about the decision that is made.³⁰³

It is therefore crucial that consumers should have a clear understanding of whether they are receiving advice or guidance, and the extent to which they are able to seek redress if things go wrong.

161. There is a clear distinction in financial services between regulated advice and guidance. Although what was proposed was clear in the Budget Red Book and in the consultation document, the Chancellor’s Budget statement on this point could have been better phrased.

162. The guidance made available to consumers must explain what, if any, protection they may have in cases of poor guidance.

When should guidance be made available?

163. Consumers approaching retirement are likely to use a range of sources to help them make decisions. The time at which guidance is offered is likely to affect the extent to which consumers benefit from that guidance and the level of influence it has on their decisions. The ABI’s current practice is to begin communicating with customers approaching retirement 12 months in advance of their stated retirement date. Otto Thoresen told us:

I think there is a tendency at the moment in this discussion to have in one’s mind the idea that this happens about a week before you retire. The retirement code that we have been running within the ABI starts a year before. This process has to start earlier.³⁰⁴

164. The greater opportunity and complexity that many people are anticipating within the retirement market means that financial decisions are no longer a ‘one-off’ occasion. Instead, many retirees will be responsible for managing their finances as their requirements and circumstances change throughout their retirement. Jane Vass of Age UK emphasised the need for ongoing advice throughout retirement:

302 Q257

303 Q264

304 Q487

If you are not taking an annuity, there is an initial decision to make, but then you will need to look at your finances regularly. There needs to be some provision for ongoing advice that potentially links up with advice earlier in life.³⁰⁵

Dr Ros Altmann suggested that guidance should be delivered while people are still in employment, and that this could be achieved by linking it to auto-enrolment. She explained:

I would expect that this could be facilitated in the workplace alongside auto-enrolment. We are basically talking about financial planning and if there was some mechanism to incentivise employers, who have to put people into pension schemes anyway, to help them with this kind of financial planning and then perhaps trustees, I think that could be helpful.³⁰⁶

165. The guaranteed guidance must be available to people well in advance of their retirement to help their decision-making.

Developing the guidance guarantee and the Money Advice Service

166. The Government's consultation paper states that, in developing the standards for guidance, the FCA will work "in close partnership with consumer groups, the Pensions Advisory Service, and the Money Advice Service".³⁰⁷

167. Our own inquiry into the Money Advice Service, on which we reported in December 2013, left us with serious concerns about the way in which the MAS was carrying out its role.³⁰⁸ We considered carefully whether to recommend that the MAS be abolished. We recommended instead that the Treasury commission an independent review of the MAS, and that this review should report by summer 2014. The then Financial Secretary to the Treasury, wrote to us on 2 February 2014 to say that the Government had accepted our recommendation for an independent review.

168. Given that the Money Advice Service has been asked by the Treasury to play a role in developing the standards for financial guidance at retirement, it is even more important that the independent review of the MAS is completed quickly.

Who should deliver the guidance guarantee?

169. The Government's consultation paper says that it will introduce a "new duty on pension providers and schemes to deliver this 'guidance guarantee' by April 2015".³⁰⁹ It also, however, requires that the guidance should be impartial. Otto Thoresen said that there was scope for third party organisations to deliver the guidance on behalf of firms:

305 Q283

306 Q286

307 HM Treasury, Freedom and choice in pensions, [Cm 8835](#), March 2014, para 4.13

308 Seventh Report of Session 2013–14, *Money Advice Service*, [HC 457](#)

309 HM Treasury, Freedom and choice in pensions, [Cm 8835](#), March 2014, p.3

I think the industry could deliver this; I have no doubt about that. We could deliver this, and deliver it cost-effectively. However, the test we would have to pass is one of genuine and demonstrable impartiality.³¹⁰

I think my members—the insurance companies—would say that they have built strong relationships with our customers and they would want to continue to service those customers well. However, there are a number of ways that we could choose to try to deliver this cost-effectively and consistently, which perhaps would lend yourself to being a bit more radical about the way you think about doing this. We already have a couple of vehicles out there that have been built. The Money Advice Service has had some challenging interrogations from this group and a sub-committee of this group, but the Pensions Advisory Service is also a very strong organisation. There must be ways that we can also use existing capability to get there faster than if we have to build it all from scratch.

[...]

If it was delivered through a third party or a utility, it would be far more straightforward.³¹¹

For her part, Dr Ros Altmann was clear that providers should not deliver guidance, saying:

The FCA needs to get to grips with how we can deliver cost-effective, impartial guidance or advice that has minimum standards and no product sale link at all. The idea that some insurance companies suggested straight after the budget that their own sales staff or telephone operators, whatever they are called, could provide this guidance is a non-starter for me. This has to be independent.³¹²

170. It is essential for the success of the pensions reforms that the guidance offered under the guidance guarantee is trusted by those who use it. The guidance offered under the guarantee must therefore be demonstrably impartial. It must certainly not be biased in favour of any particular product type or provider.

Who will pay for the guidance guarantee?

171. In the Budget the Chancellor provided £20m over the next two years to fund the creation of the guidance guarantee.³¹³ The Chancellor described this as:

Literally a development fund, to develop over the coming year the guidance package [...] then, of course, going forward the guidance will be a cost borne by the industry and I think that is understood.³¹⁴

310 Q493

311 Q491

312 Q282

313 Office for Budget Responsibility, Economic and fiscal outlook, March 2014, p 179, Table A.1

314 Q422

In his Budget speech the Chancellor said the guidance service would be free.³¹⁵ He clarified this statement in evidence to us, saying that the guidance would be:

Free at the point of use, so that costs will be borne by companies, by the industry, and that are one of many costs of doing business. I think it is more than outweighed by the benefits to the industry of what I am offering.³¹⁶

172. The running costs of the guidance will be determined by the form it takes and who delivers it. Some estimates put the potential costs as high as £120million a year.³¹⁷ The ABI said this “would not seem an unreasonable estimate” and the NAPF said “it looks like it might be in the right ballpark”.³¹⁸ There was also agreement between NAPF and APFA that these costs would ultimately be passed on to the consumer.³¹⁹ Otto Thoresen told us that “It will have to be paid for, and it will be paid for by the customer in the end.”³²⁰

173. It will be important for the success of this policy that people receive high quality guidance. As well as being of value to the individual it will have public policy benefits. People need to be aware that while the guidance is to be free at the point of use, the costs of firms providing it will borne by consumers. It is crucial that people grasp the value of this guidance. We therefore recommend that the full average cost of the provision of the guidance by firms be estimated and disclosed to consumers.

Interaction with existing and proposed Government sponsored guidance

174. The ‘guidance guarantee’ for those approaching retirement is not being created in isolation. The Money Advice Service and Pension Advisory Service have existed for some time. The Government has also legislated to ensure local authorities provide “comprehensive information and advice about care and support services in their local area” in the provision of long-term care.³²¹

175. The aim of the guidance will not be final product selection. As the FCA described:

I think the purpose of the guidance would be to put those questions in people’s minds. As I say, it can’t decide the product for them but what it can do is tell people the implications of various decisions, “If you choose to take the money and you run out of money then effectively that is a decision for you and, equally, the implications of things like people on average live for X years and so on from your age”, and put those thoughts, where it is factual, in people’s minds.³²²

315 HC Deb (2013-14), 19 March 2014, col 793

316 Q423

317 PricewaterhouseCoopers, Budget 2014 – Annuity reform, key implications for the insurance industry, March 2014

318 Q489; QQ340

319 Q335; Q327

320 Q482

321 Department of Health, Factsheet 1: The Care Bill - General responsibilities of local authorities: Prevention, information and market-shaping, December 2013

322 Q266

176. Age UK said that “there are overlaps with advice for care” and that it was important to link between existing providers in order to offer retirees a comprehensive service:³²³

It will be important to link up web advice from people like the Money Advice Service through to telephone advice from the Pensions Advisory Services through to more detailed face-to-face advice. That will need a very strong framework. It will need strong standards but, very importantly, it will also need good ways of handing off people between the different parts of the system.³²⁴

177. Age UK also called for guidance to go further than currently envisaged:

Guidance, in this area, may need to go much further than just the financial issues. For example, issues around whether or not you should retire at all; what to do about housing or debt; the factors you need to take into account. Guidance has a very clear role to play in that, but guidance also has a role in telling people when they should be taking regulated advice.³²⁵

178. The ‘guidance guarantee’ is not the only Government sponsored guidance being designed for pensioners or those who are approaching retirement. These schemes should operate in concert to help people make informed decisions about what is right for them in retirement.

From guidance to advice

179. The provision of guidance, and the complexity of the new market, is likely to trigger a greater requirement for further support and financial advice. The FCA also acknowledged this:

What that will not be and what will still be the case for many people, I suspect, is that it is then appropriate for them to go on and get their own independent Advice.³²⁶

180. An increased demand for products, in what will be a more complex market, is likely to also increase demand for professional financial advice. Joanne Segars told us that there was already a problem with the affordability of that advice:

Very many people simply cannot get that advice. The pension pots are too small for them to be profitable for advisers or brokers to want to deal with and that is not just a problem for individuals. It is a problem for small trust-based pension schemes trying to put annuity broking services together or trying to provide support to their scheme members.³²⁷

Chris Hannant, Director-General of the APFA, acknowledged this problem, saying: “I know there are firms out there who can provide advice cost-effectively at pension pots less

323 Q284

324 Q285

325 Q283

326 Q261

327 Q335

than £10,000, of about £5,000, but there is a problem at the bottom end.” On the question of whether there was sufficient capacity in the advice market to cope with these reforms, he told us:

If everyone who retiring next year was to seek full advice I think there would probably be a challenge on capacity. [...] It is a question of scaling up. There would need to be a clear signal early in terms of what is expected in terms of the industry to prepare. I believe there is scope in the industry to deliver advice more cost-effectively through the use of more junior staff and overseen by fully-trained, qualified advisers.³²⁸

181. Otto Thoresen expected that there would be an increase in demand for advice, but suggested the prospect of new technologies creating additional capacity and the potential to bring down costs:

This change will increase demand for regulated advice around decisions at retirement, and accelerating some of the existing work going on within the FCA about how that advice can be delivered safely and economically using new mechanisms and new technologies is an important part of making this whole system work well for society. I would like to think that we can also take that opportunity to try to move some of this stuff forward faster.³²⁹

182. The APFA similarly highlighted that:

One of the things we are seeing is greater use of technology that can help lower costs and there are some firms out there who are looking to try to provide an entire computer-generated advice process. In the future that may help, although a lot of people still want the face-to-face service. Yes, there is a challenge for our sector to become more efficient and reduce the cost of advice.³³⁰

183. The FCA is currently undertaking work to ensure regulation does not limit innovation in this area as the Treasury Committee heard in February this year:

We should encourage the innovation in this area. Ultimately we will have to take the decision, “Is this good enough?” but I do not think we should let the perfect be the enemy of the good when the fundamental problem is the cost of providing advice at all. I would rather have some good automated advice that gets to reasonably simple, understandable products than to have had hidden trail commission in the past.³³¹

184. The regulator has assured the Committee this issue will be consulted on shortly but highlighted their concerns that:

It is a real concern because the distinction between a product which is advised on the web and execution-only on the web is not a distinction that people naturally and easily can determine. We are spending quite a lot of time talking to the industry

328 Q336

329 Q492

330 Q343

331 Oral evidence taken on 4 February 2014, HC (2013-14) 1058, Q43 [John Griffith-Jones]

about whether we need to revise our guidance to make products fall very clearly into one class or the other.³³²

185. The Chancellor's commitment was for face-to-face advice to be available. Evidence to the Committee from a number of witnesses suggested a desire to use other channels. These will be appropriate for some customers but, in line with the Government's pledge, it is important that at least for those who choose face-to-face guidance this is provided without financial detriment to the customer.

Principles for the 'guidance guarantee'

186. The pension reforms announced by the Government are welcome, and also transformational. Consumers will need considerable support in navigating a market which is undergoing major change and in which consumers are likely to be offered an array of new products. The Committee recommends that the proposed guidance under the guarantee observe the following principles. It should:

- Be demonstrably impartial as to providers and type of product;
- Include at least an initial opportunity for face-to-face guidance;
- Be free at the point of use, with the costs of such provision made transparent;
- Make clear to every consumer exactly what is being offered, the limitations of the guidance, and what protection it gives consumers in the event of detriment;
- Be offered from at least 12 months in advance of the consumer's stated retirement date; and
- Be co-ordinated with Government-sponsored guidance relating to long-term care.

Impact on the wider economy

Defined benefit schemes

187. An important part of the Government's consultation is whether and to what extent these pension reforms should be open to private defined benefit scheme members.³³³ At present, members of these schemes can transfer their accrued funds by converting them into a cash equivalent transfer value.³³⁴ The Government is consulting on whether this should continue to be permitted.

188. Michael Saunders, of Citi, told us that allowing defined benefit members the right to transfer would be likely to have a greater impact on the economy than that currently anticipated within the annuity market:

332 Oral evidence taken on 4 February 2014, HC (2013-14) 1058, Q59 [Martin Wheatley]

333 HM Treasury, Freedom and choice in pensions, March 2014, pp 33-36

334 Money Advice Service, [Transferring out of a defined benefit pension scheme](#), accessed 10 April 2014

It would be basically the same effects on flows by fewer annuity purchases, potentially more spending, but on a much greater scale, because in aggregate the DB pension schemes are closer to maturity and obviously much larger than the DC schemes.³³⁵

The IFS said that the extension of the reforms could destabilise the risk-pooling of defined benefit schemes:

I think part of the issue there is that, from the beginning of the defined benefit system, you have risk sharing. For example, if I hit 60 and I am pretty ill and I think I am not going to live terribly long, I have a very big incentive to take my money out of the DB scheme and make use of this ability not to have to buy an annuity. If I do that and my DB scheme is funded on the assumption that a proportion of people will die early, which they are, then that requires additional contributions from everyone else or reduced benefits; probably additional contributions.

There is a danger of undermining the funding structure of DB schemes if you allow those who will benefit most from not having an annuity or a pension to move out early. I can understand the caution here because I think you do risk the schemes being selected against by those who do less well from the schemes. I think that is a fundamental part of the risk sharing that defined benefit schemes provide.³³⁶

189. Joanne Segars said that, while transfers are currently permitted, the impact of extending the reforms was uncertain:

Of course, at the moment people do have the right to shift their DB pot into a DC scheme and then in future they will be able to do what they want with that. At the moment, of course, they have to abide by the rules as they current exist and schemes do use that at the moment as a sort of de-risking valve, but we need to consider what the likely demand might be for members of DB schemes and what the impact might be flowing forward. As I said, at the moment it is too early to say. We are still working through those numbers with our members.³³⁷

She also said that the reforms would require changes within the schemes' asset management and that the NAPF would need to work with schemes and the Treasury to model the impact:

We need to work with our members to find out and work through what the impact would be on pension funds' investment policies if these changes were extended to defined benefit pension schemes. At the moment, I think it is too early to tell. We need to crunch through the numbers. We need back from Treasury some of their modelling so that we can work with the Treasury to help understand what the impact might be.³³⁸

335 Q51

336 Q67

337 Q320

338 Q305

Changes in consumption and asset allocation

190. The greater choice that the pension reforms allow is likely to lead to changes in the investment and consumption patterns of people in retirement. Economists from whom we took evidence did not predict any damaging consequences to the macroeconomy from these reforms, but did suggest that they might have an effect on specific markets. Robert Wood, of Berenberg Bank, said:

I think it would be a small positive for consumption. Frankly, I don't know how big the number would be but I think directionally it would be positive for consumption.³³⁹

One key question is how much money flows into the housing market in one way or another now these funds can be allocated to different investments other than just annuities, and of course the gilt market.³⁴⁰

Michael Saunders, of Citi, agreed with this assessment for the short term, but suggested that the economic impacts of the changes might not be felt for some time:

The effects near term on the economy are small but they build over time because most of the DC schemes are not yet at the point where people are retiring off them. You can see that the flows out of them would be much larger if you go forward 10 or 20 years.³⁴¹

191. The principal cause of the OBR's uncertainty was the ability of consumers to transfer between assets quickly:

One reason to underline the uncertainty here is how quickly people can move relatively large amounts of money from one form of holding wealth to another.³⁴²

192. The FCA warned that where customers concentrate their wealth in one asset class they increase their investment risk:

If you have a strong level of investment into the wider property market, there are issues there if people are over-extending into that space. Clearly, for someone who is taking a pot in cash under potentially these reforms, one of the questions you think about, whatever they are investing in, whether it is property as buy-to-let or whatever it might be, is what the overall balance of risk is they are taking. Clearly, in any product, someone who says, "Great, I am going to take all of my pot and I am going to put it all into one thing", is running an awful lot of risk and, if you had a significant amount of money to invest in those circumstances, we would want them to consider taking independent advice.³⁴³

339 Q48

340 Q48

341 Q50

342 Q206

343 Q255

193. Reliance on housing as a single investment asset class may be of concern as house prices have a history of peaks and troughs. This volatility was evident when average UK house prices fell by 20 per cent, from £186,044 to £147,746, in the sixteen months between October 2007 and February 2009.³⁴⁴ Similarly, at the beginning of the 1990s, the Nationwide House Price Index recorded a fall of 20 per cent between Q3 1989 and Q1 1993.³⁴⁵ Following this fall, prices did not begin to recover until the beginning of 1996.³⁴⁶ As discussed earlier, regional variation also affects house prices. House prices remain 22 per cent below their inflation-adjusted peak across the UK, but only 6 per cent below their peak in London.³⁴⁷ The impact of inflation and changes in rents may add further complexity and uncertainty to any assessment of the returns available on housing as an investment.

194. When asked about the potential risk of over-investment in housing the Chancellor said:

The OBR was aware of the policy when they did the house price forecasts and the impact of buy-to-let historically, although you made the point about the future, has been a bit more limited than perhaps the hype would lead you to believe on house prices. But as I say, I don't think that would be a reason to not go ahead with pensions flexibility.³⁴⁸

195. There are risks to individuals and the wider economy if people decide to concentrate their savings in a single asset class such as residential property. Contrary to widespread perception, residential property can be a volatile asset class and prone to large falls in value.

Future infrastructure investment

196. Annuity providers and pension funds are intended to be important sources of long-term investment for the UK economy. The Government has a target of securing £20 billion of investment over the next decade.³⁴⁹ The Chancellor acknowledged the UK's structural weakness in generating future infrastructure investment:

There is a structural issue for the UK and there are a whole range of things that we can do to try to improve that, such as reforms in the financial system, to the way things are financed [...] by trying to get pension funds invested in infrastructure.³⁵⁰

197. We asked witnesses whether the pension reforms announced in the Budget might have an effect on infrastructure investment. Robert Wood, of Berenberg Bank, suggested that the effects would not be felt for some time:

344 "House prices continue to fall in February", The Guardian, 26 February 2009

345 [Nationwide house price index data](#) - UK Series

346 [Nationwide house price index data](#) - UK Series

347 [Nationwide house price index data](#) and ONS consumer prices dataset, February 2014, series [D7BT](#)

348 Q405

349 HM Treasury, [Government welcomes first injection into Pensions Infrastructure Platform](#), 18 October 2012, accessed: 9 April 2014

350 Q371

Infrastructure spending is one thing that exercises a lot of people, given that part of the plans for the next few years was to have the providers of these annuities, these pension providers, allocating funds to help infrastructure. This money won't just disappear—people currently have a lot of money invested in annuities—but it does mean that over the next 20 or 30 years, presumably as flows into annuities fall, that pot of money available will also become less significant.³⁵¹

Joanne Segars told us that there would not be an immediate impact on investment, saying: “For the moment our members remain very interested in investing in infrastructure”.³⁵² For his part, Otto Thoresen thought that “there will be an impact on infrastructure and insurer investment in the wider economy in the years ahead.”³⁵³

198. The Chancellor believed that support for infrastructure was unaffected following the announcements of these reforms:

The encouraging response I have had from my own conversations with leading players in the industry is that they are still interested in investment in infrastructure because of the predictable and stable returns that that can provide.³⁵⁴

Relationship to other savings reforms

199. The Budget announced the introduction of a New ISA (NISA), which will be “a simpler product with equal limits for cash and stocks and shares”, to be introduced from July 2014. The annual investment limit for the NISA will be £15,000 a year for both cash and stocks and shares, and savers will be able to transfer previous years' funds from stocks and shares ISAs into cash ISAs. The Government also announced that peer-to-peer loans would be eligible to be held in ISAs, and that all restrictions around the maturity dates of securities held within ISAs would be removed.³⁵⁵

200. These changes amount to a considerable increase in the flexibility of ISAs. Taken together with the increase in the flexibility of defined contribution pensions, they suggest that the lines between pensions and other kinds of saving are becoming blurred. David Geale of the FCA told us:

I think people have always been able to look at different methods of saving for their retirement and pensions should not be seen as exclusively that route. Is it becoming more so? Yes, I think that is right, with greater flexibility. There is also the hope that people may save more over that period, be that through ISAs, pensions or other routes.³⁵⁶

351 Q48

352 Q304

353 Association of British Insurers, Briefing from the Association of British Insurers: Budget 2014, 24 March 2014, p 6

354 Q411

355 HM Treasury, Budget 2014, [HC 1104](#), 19 March 2014, paras 1.167–1.169

356 Q268

Table 6: Pension schemes – annual and lifetime allowances since their introduction, £ thousands

	Lifetime allowance	Annual allowance
2006-07	1,500	215
2007-08	1,600	225
2008-09	1,650	235
2009-10	1,750	245
2010-11	1,800	255
2011-12	1,800	50
2012-13	1,500	50
2013-14	1,500	50
2014-15	1,250	40

Source: HMRC

201. Changes made to the allowances and reliefs applied to pensions in recent years have made it more likely that people will suffer through paying tax more than once (sometimes known as double taxation) on the income they use to finance pension saving in the first place, the capital gain or interest on that money, or the income received subsequently from the pension. In particular, the introduction in 2006 of annual and lifetime pension allowances, and their recent substantial reduction (see Table 6), have limited the amount of pension a person can save which is eligible for tax relief. This will have increased the amount of income subject to such ‘double taxation’.

202. Nor have changes to the pensions taxation regime removed the fact that some income attracts no tax at all when it is saved towards a pension. The tax-free pension commencement lump sum (usually up to a quarter of an individual’s pot) will continue to be available following the implementation of the Budget changes, as will the exemption from national insurance contributions applied to payments made by employers into pension schemes. For her part, Joanne Segars broadly agreed with the principle of savings being taxed only once, but favoured keeping the tax-free lump sum. She told us:

We would certainly want to keep some that is not taxed at all, yes. We would like to have rather more of it that is not taxed, but we would certainly like to keep the tax-free lump sum because, again, if we are talking about the incentives for people to save for retirement in the first place, that is a big incentivisor.³⁵⁷

203. Mr Mortimer-Lee noted that pensions saving was effectively subsidised over other forms of saving:

One of the questions I have about this is in the past you got a tax break and the quid pro quo was you had to invest it in a pension in the form of an annuity. Now that you don’t have to invest in an annuity, what is the rationale for the tax break? What makes this form of saving tax privileged? I think there are a number of questions that

are raised. One is DB versus DC schemes and the other is why are we tax subsidising this form of saving and not all other forms of saving?³⁵⁸

Gemma Tetlow spelled out in more detail the tax advantage offered to pension saving:

The thing to be clear about is exactly what we mean by the more tax-favoured bit of pension saving. You do not pay any tax on your contributions to a pension. You do not pay any tax on the investment returns in your fund, but then you pay tax on the way out. Most of that we would not think of as over-generous tax-favouring of pension saving. There are strong reasons, as outlined in the *Mirrlees Review*, for not taxing the normal return on savings and ISAs have a similar feature, although they are taxed and then exempt in the two other places.

It is not that bit of tax treatment of pensions that we were focusing on as being more generous than other forms of saving. It is other elements, such as the fact that employer contributions to pension schemes avoid all national insurance contributions as well, which obviously never get charged on the way out either, and the fact that you can take 25% of your pension fund completely tax free. That is 25% that never gets taxed at any point. It is those elements that seem much more generous relative to any other form of savings vehicle that you could think of.³⁵⁹

Paul Johnson, Director of the Institute for Fiscal Studies, argued that:

We would not suggest that [...] pensions should be taxed very heavily. They should not be taxed twice. It is just that they should be taxed once and, as Gemma said, the case for taking a quarter of it up to £300,000 or something, completely tax free—never been taxed on the way in, not taxed when it is there, not taxed on the way out—has always looked a little difficult but, given that you can now take this as a lump sum anyway and pay normal tax, the case for that is probably reduced. I think it is important to be terribly clear that we are not suggesting with any of this that we want to move away from or that the Government should want to move away from exempting from tax contributions on the way in because that is just part of a—

Mr McFadden: Exempting pensions from tax contributions.

Paul Johnson: Exactly, because I think that is just part of sensible system for taxing savings; you are only taxed once and you are taxed on the way out. That seems like an appropriate way of taxing savings.³⁶⁰

204. Robin Fieth, Chief Executive of the Building Societies Association, thought that there was merit in the principle that people should be taxed only once on their savings.³⁶¹ Chris Hannant, Director-General of APFA, broadly agreed with this, but added:

The ISA currently will offer far more flexibility, but I think it is right that people are nudged towards a framework for the long term so it is there until you are 55. I also

358 Q51

359 Q53

360 Q64

361 Q352

think the taxation on the drawing down rather than paying in is important. Good tax planning will help negate the Lamborghini problem because it will be you are better off spreading that pension pot over a number of years rather than taking it all at once.³⁶²

205. Taken together, the changes announced in the Budget to ISAs, as well as the reforms to the taxation of defined contribution pensions at retirement, amount to a substantial increase in the flexibility available to savers. As this flexibility increases, ISAs and pensions will become increasingly interchangeable in their effect. In the light of this, the Committee recommends that the Government set out comprehensively the approach it intends to take to taxation of all forms of saving. This should include an examination of the merits of moving further towards taxing savings once, the scope for bringing closer together the tax treatment of ISAs and pensions, and the appropriateness of the present arrangements for the pension tax free lump sum.

Pensioner bonds

206. The Budget announced that National Savings and Investments (NS&I) would “launch a choice of fixed-rate, market-leading savings bonds for people aged 65 or over, available from January 2015 and allowing inflows of up to £10 billion.”³⁶³ For the purposes of costing this measure, the central assumption made in the Budget was “that NS&I will launch a 1-year bond paying 2.8% gross/annual equivalent rate (AER) and a 3-year bond paying 4.0% gross/AER, with an investment limit of £10,000 per bond.”³⁶⁴ The Government will announce precise details of these bonds in the Autumn Statement later this year, taking account of the “prevailing market conditions at that time”.³⁶⁵ The Government also announced that NS&I’s Net Financing target would be increased:

NS&I will have a net financing target of £13.0 billion in 2014–15, within a range of £11.0 to £15.0 billion. This will allow NS&I to support savers with a choice of fixed-rate market leading savings bonds for people aged over 65 from January 2015, taxable at the marginal rate, and raise the Premium Bond limit from £30,000 to £40,000 from 1 June 2014.³⁶⁶

207. This announcement seems to amount to a change to the way in which the rates on NS&I savings products are set. NS&I’s own website describes the process for setting its rates as follows:

We set our rates to balance the interests of three groups: our customers—offering them a fair rate; taxpayers—with our remit to raise cost-effective finance for government; and the wider financial services sector—supporting stability.³⁶⁷

362 Q354

363 HM Treasury, Budget 2014, [HC 1104](#), 19 March 2014, para 1.173

364 HM Treasury, Budget 2014, [HC 1104](#), 19 March 2014, para 1.173

365 HM Treasury, Budget 2014, [HC 1104](#), 19 March 2014, para 1.173

366 HM Treasury, Budget 2014, [HC 1104](#), 19 March 2014, para C.11, p. 102

367 National Savings and Investments, [What we do](#), accessed 9 April 2014

We took evidence from the Chief Executive of NS&I, Jane Platt, and its Partnership Director, Steve Owen, on 4 March—two weeks before the Budget. We asked Jane Platt whether encouraging saving was part of NS&I’s remit. She told us:

That is no longer there in terms of the objectives or the operating framework of NS&I. We are now tasked with balancing the interests of the customer, the taxpayer and broader financial stability.³⁶⁸

She described this as the “balance of three”.³⁶⁹

208. In the light of NS&I’s responsibility to its customers, we asked why NS&I had reduced the rate offered by its Direct ISA from 1.75 per cent to 1.5 per cent. Jane Platt told us:

We decided to cut it because if we had left it where it was [...] we would have been at the top of the market and we are not positioning our products at the very top of the top quartile on the usual basis.³⁷⁰

On the question of why NS&I had withdrawn index-linked savings certificates, she said:

The last time we had index-linked savings certificates on sale was not this summer but the summer before. We put an offer on sale that was planned within the context of the net financing envelope that we had for that particular year, so we were able to have index-linked savings certificates on sale for close to four months. During that period we raised the amount of money that we had wanted to raise, and then closed the offer.³⁷¹

We understood these answers to mean that NS&I was prevented from offering market-leading rates and products, which would be in the interests of its customers, by the other two elements of the “balance of three”: the constraints of its net financing target and—to a lesser extent—the interests of the wider financial services market.

209. The Government’s Budget policy costings document acknowledged that the cost of raising finance through NS&I would be greater than the cost of usual borrowing decisions:

The costing is calculated by estimating the increased cost of the NS&I product over usual borrowing decisions, which it is assumed would raise the money through a mixture of Gilts and T-bills. This is the difference between a pre-measure scenario where the government raises £10 billion through the DMO, and a post-measure scenario where £10 billion is raised through the new NS&I bonds rather than through gilts.³⁷²

210. We asked Robin Fieth, Chief Executive of the Building Societies Association, what effect the introduction of these bonds would have on other providers in the savings market:

368 Oral evidence to the Treasury Committee, National Savings and Investments, [HC \(2013-14\) 1131](#), 4 March 2014, Q8

369 Q21

370 Oral evidence to the Treasury Committee, National Savings and Investments, [HC \(2013-14\) 1131](#), 4 March 2014, Q15

371 Oral evidence to the Treasury Committee, National Savings and Investments, [HC \(2013-14\) 1131](#), 4 March 2014, Q17

372 HM Treasury, [Budget 2014: policy costings](#), March 2014

[...] there are some imponderables in that. If we start at the headlines and go slightly wider than the pensioner bonds, if I may, to the NS&I target for the next year of £13 billion. If we took that as the share of net cash savings market for the current year, on our assessment it is about 25% of the net cash savings market. It is a fairly large chunk and when you then look at the rates that the pensioner bond is offering, which are markedly higher than the best rates available for similar products in the market at the moment, then we can certainly anticipate some impact on the savings market.³⁷³

On the question of whether the introduction of “pensioner bonds” would increase household savings, he suggested that “past experience says that it probably will not have a huge effect”.³⁷⁴ We asked what the effect on building societies would be if people over 65 chose to move existing savings into pensioner bonds. He told us:

That is certainly one of the scenarios we are considering and not just building societies because it is the banks as well. The question is, how do the banks and building societies respond in terms of attracting savings? Perhaps the most important factor for building societies in this is that they are required by law to be at least 50% funded through retail deposits and most, of course, are much higher than that. Most are in the 70% to 100% level. Will they have to put up savings rates in order to attract sufficient cash and retain sufficient cash? Of course, the flipside of that is whether that will have an impact on mortgage rates because the only other consequence is it has an impact on profits, which is therefore the building up of reserves in order to lend more in the following year. There is a whole equation to balance there.³⁷⁵

For her part, Dr Ros Altmann thought that the introduction of these bonds might “throw down a challenge to the industry, ‘If you want to get some good pensioner money in you have to beat the pensioner bonds’”.³⁷⁶

211. The Government’s announcement that National Savings and Investments (NS&I) will offer ‘pensioner bonds’ at a market-leading rate represents something of a departure from NS&I’s usual approach. NS&I is required to balance the funding needs of the Government, its customers and the wider financial services sector. Pensioner bonds have tilted this balance—in this case at least—in favour of customers and away from the Government and the financial services sector. The Government must provide clarity about the framework within which NS&I is now operating.

212. Since the Government has decided that it wants NS&I to give priority to customer interests, we recommend that NS&I consider once again offering index-linked savings certificates.

213. The increase of NS&I’s Net Financing Target from £2 billion, plus or minus £2 billion, in 2013–14 to £13 billion, again plus or minus £2 billion, in 2014–15 could have a significant effect on NS&I’s market share. The Government must ensure that this

373 Q344

374 Q345

375 Q346

376 Q287

does not destabilise the wider savings market by crowding out private savings providers.

5 Taxation

Principles of taxation

214. In March 2011, the Committee published a Report, *Principles of Tax Policy*, in which we set out six principles with which tax policy should comply. These are:

- Basic fairness;
- Supporting growth and encouraging competition;
- Certainty, including simplicity;
- Stability;
- Practicality; and
- Coherence.

This year the Committee has again asked the three professional tax bodies—the Association of Certified Chartered Accountants, the Institute of Chartered Accountants of England and Wales, and the Chartered Institute of Taxation—to assess how far the main tax principles contained within the Finance Bill comply with these principles. This is the third year professional bodies have made this assessment and their submissions are contained in Appendices 1, 2 and 3.

215. When asked about the Government’s progress against the six principles of tax policy Patrick Stevens, Tax Policy Director, Chartered Institute of Taxation, told us:

[...] my personal view is that some things have improved and some things have got worse. I actually think that they moderately cancel each other out. What has improved, I think, is the method of making law, by which I mean there is now a much longer and more detailed consultation process for detailed tax law. It generally lasts for in excess of a year, where you have a succession of consultations.³⁷⁷

He went on to explain that there were two areas which were not improving. First, there had been an increase in the use of retrospection in the tax system. Secondly, more taxpayers were being taxed by statute and untaxed by guidance.³⁷⁸ He argued that this meant that new legislation was being introduced which was too wide-ranging. As a result HMRC had to produce guidance, which could be changed at its discretion, in order to narrow down the application of the law. Mr Stevens explained that this gave HMRC the “power to make their own guidance and therefore their own law”.³⁷⁹ Frank Haskew, Head of Tax Faculty, Institute of Chartered Accountants in England and Wales, largely agreed:

377 Q496

378 Q498

379 Q515

To emphasise, we have a better consultation process I think, but looking at the Treasury Committee's principles, we do see that we still have very long, hugely lengthy, complicated Finance Acts and, [...] there is a lot of uncertainty in some of those provisions.³⁸⁰

216. Our report on the *Principles of Tax Policy* said that there were substantial benefits to be had from a tax system that was “simple, understandable and clear”.³⁸¹ Mr Haskew explained that the Government had not achieved simplification:

I was actually in front of this Committee a few years ago with John Whiting when it was stated that the Government had taken out about 100 pages of tax legislation, with the Office of Tax Simplification work, but in fact they had added a 400-page Finance Act at the same time, so the net result was plus 300. Since then we have had the longest Finance Act in history last year, and we had an almost 600-page Bill put in front of us a week ago.³⁸²

We consider below some of the individual policy measures announced in the Red Book and how they performed against the Committee's principles of tax policy.

Retrospection and anti-avoidance

217. When the Committee last reviewed this area of the tax system in our Budget 2012 Report, we recommended that:

[...] the Government restrict its use of retrospective legislation to wholly exceptional circumstances, which should be narrow and clearly-defined. The Treasury should set these out as soon as possible for consultation, along with an explanation of how gradual further extension of retrospection can be prevented. Any future retrospective tax measure must be justified against the agreed criteria: such justification must include clear explanatory statements to Parliament by the responsible Minister and should invite views from relevant professional bodies.³⁸³

218. We questioned the three professional tax bodies on whether the Government was abiding by this recommendation. Mr Stevens said this had not been “wholly achieved” by the Government.³⁸⁴ Mr Haskew told us:

I think we wholly welcomed [the Committee's recommendation] at the time. In terms of where we are today, I think I would struggle to say that the Government is abiding by those Treasury Committee recommendations.³⁸⁵

219. In his speech to the House, the Chancellor said that “while the vast majority of wealthy people pay their taxes, there is still a small minority who do not”.³⁸⁶ He announced

380 Q499

381 Treasury Committee, Eighth Report of Session 2010–12, [Principles of Tax Policy](#), HC 753, p 28

382 Q501

383 Treasury Committee, Thirtieth Report of Session 2010–12, [Budget 2012](#), HC 1910, para 89, p 39

384 Q545

385 Q546

386 [HC Deb 19 March 2014 c792](#)

that the Government “will now require those who have signed up to disclosed tax avoidance schemes to pay their taxes, like everyone else, up front”.³⁸⁷ The Red Book sets out that:

Tax avoidance scheme promoters must give HMRC information about schemes they promote under the Disclosure of Tax Avoidance Scheme (DOTAS) rules. Anyone using such a scheme must declare to HMRC they are using a notified tax avoidance scheme. Following consultation, this Budget announces that the government intends to extend the new requirement for taxpayers to pay upfront any disputed tax associated with schemes covered by the DOTAS rules or counteracted under the General Anti Abuse Rule (GAAR).³⁸⁸

This policy will provide HMRC with additional tools to retrospectively “address a legacy stock of an estimated 65,000 avoidance cases”.³⁸⁹ The requirement for taxpayers to pay upfront any disputed tax will remove the “cashflow advantage” for the taxpayer of holding onto the tax during the avoidance dispute. If the taxpayer subsequently wins their case in the courts, they will be reimbursed with interest.³⁹⁰

220. The OBR has forecast that the Government’s accelerated payments policy will raise £4 billion in tax receipts over the forecast period to 2018–19.³⁹¹ In its evidence to the Committee, the ICAEW said that “if past experience is a guide, these estimates may well prove to be optimistic.”³⁹² On the other hand, Mr Stevens told us that he found the £4 billion figure “credible, compared to some of the other estimates I have seen over the years on what the results of anti-avoidance legislation will be”.³⁹³

221. The Government’s *Budget 2014: policy costings* document described how this figure is calculated. The estimate is based on the total value of tax under dispute by HMRC related to marketed, artificial avoidance cases which is “around £14 billion, associated with a population of around 65,000 taxpayers”.³⁹⁴ A £2.5 billion downward adjustment is made relating to anti-avoidance cases outside the scope of this Budget measure. A number of other adjustments are then made, including the assumption that HMRC has an 80 per cent win rate in anti-avoidance cases.³⁹⁵

222. In response to a request made by this Committee, the Treasury provided additional information on the behavioural responses:

By removing the cash-flow advantage arising from entering into avoidance schemes, HMRC expect the accelerated payments measure to reduce the use of such schemes in future. The issue of behavioural responses does not apply to the stock of

387 [HC Deb 19 March 2014 c792](#)

388 HM Treasury, [Budget 2014](#), 19 March 2014, para 1.200–1.201, p 52

389 HM Treasury, [Budget 2014](#), 19 March 2014, para 1.200–1.201, p 52

390 HM Treasury, [Budget 2014](#), 19 March 2014, para 1.200–1.201, p 52

391 OBR, [Economic and Fiscal Outlook](#), 19 March 2014, table A.1, p 181

392 ICAEW, [written evidence](#)

393 Q524

394 HM Treasury, [Budget 2014: policy costings](#), 19 March 2014, p 36

395 HM Treasury, [Budget 2014: policy costings](#), 19 March 2014, p 36

outstanding avoidance cases, which account for the majority of the yield. Rather it concerns taxpayers who would have otherwise used avoidance schemes in the future.

[...] HMRC assume taxpayers fall into one of three categories:

- Those who continue to use avoidance schemes in future and will have to make accelerated payments;
- Those who stop using avoidance schemes altogether and become fully compliant; and
- Those who stop using these schemes, but find alternative routes to lower their tax bill either through tax planning or other artificial arrangements outside the scope of accelerated payment measures.³⁹⁶

223. The Government's *Budget 2014: policy costings* document identified a key area of uncertainty surrounding this policy:

The profile of the yield from the accelerated payments [...] measure is dependent on a large number of assumptions, some of which again concern the behavioural response of those affected.³⁹⁷

224. The Government's accelerated payments policy was consulted on between 24 January 2014 and 24 February 2014.³⁹⁸ Mr Haskew told the Committee that "four weeks is not a long time".³⁹⁹ Mr Courts expressed further concern by saying that it was not just the length of the consultation which was a problem, but also the timing because January is the "busiest time for practitioners and also corporate reporting".⁴⁰⁰

225. Retrospective tax legislation conflicts with the principles of tax policy recommended by this Committee. In our Budget 2012 Report we recommended that the Government restrict the use of retrospection to wholly exceptional circumstances. Witnesses told us that the Government was not abiding by this recommendation. Furthermore, the Red Book announced an additional retrospective taxation policy: an extension of the requirement for taxpayers to pay upfront any disputed tax associated with anti-avoidance schemes. This policy will retrospectively apply to some of the 65,000 outstanding tax avoidance cases. There may be a case for this policy but the Government has yet to explain what is wholly exceptional about these cases that justifies this retrospective measure. It should do so in response to this Report.

HMRC debt recovery powers

226. In his Budget speech, the Chancellor said that public tolerance for people who do not pay their fair share of taxes "evaporated long ago".⁴⁰¹ He announced that HMRC would be

396 Letter from David Gauke to the Chairman of the Treasury Committee, 9 April 2014

397 HM Treasury, [Budget 2014: policy costings](#), 19 March 2014, para B.9, p 67

398 HMRC, [Tackling marketed tax avoidance: summary of responses](#), March 2014, para 1.1, p 5

399 Q525

400 Q531

401 [HC Deb 19 March 2014 c792](#)

given “modern powers to collect debts from bank accounts of people who can afford to pay but have repeatedly refused to, like most other Western countries.”⁴⁰² The Red Book states that:

The government will modernise and strengthen HMRC’s debt collection powers to recover financial assets from the bank accounts of debtors who owe over £1,000 of tax or tax credit debts, have the financial means to pay, and have been contacted multiple times by HMRC to pay. A minimum of £5,000 will be left across debtors’ accounts. This brings the UK in line with many other tax authorities which already have the power to recover debts directly from an individual’s account, such as France and the US.⁴⁰³

227. In his evidence to the Committee, the Chancellor provided additional detail about the circumstances when HMRC would access people’s accounts. He said that the power would apply to people who had been “contacted on average nine times by the Revenue”⁴⁰⁴ and had exhausted all other appeals. He told us that “over half of the people affected will have more than £20,000”⁴⁰⁵ in their bank accounts and a 14 day notice period would be given before money was collected from bank accounts. He told the Committee that this new policy was simply a modernisation of existing powers:

These are people who have exhausted all the appeals, been given many warnings and are finally told they have 14 days to pay up and we would send, at considerable cost, the bailiffs round to seize their physical assets. We are introducing a new power used across Europe and across the Western world to say that instead of sending the bailiff round, we will take the money direct from a bank account with money in it.⁴⁰⁶

228. Under HMRC’s current powers, if a taxpayer has an outstanding tax payment, HMRC can legally take possession of goods in a process referred to as Taking Control of Goods, sometimes known as ‘distrain’. Taking Control of Goods is an enforcement process by which HMRC can seize a taxpayer’s possessions and sell them at auction in order to settle an unpaid tax bill.⁴⁰⁷ This process is usually conducted by a HMRC field officer, not a bailiff working for a debt collection agency. A bailiff can be appointed on behalf of HMRC by a magistrates court or a county court, after the Taking Control of Goods enforcement action has been unsuccessful.⁴⁰⁸

229. HMRC has the legal power to seize a taxpayer’s possessions without a court order. However, the HMRC field officer cannot force entry into the premises without a warrant which has to be obtained from a Justice of the Peace.⁴⁰⁹ HMRC’s Debt Management and

402 [HC Deb 19 March 2014 c792](#)

403 HM Treasury, [Budget 2014](#), 19 March 2014, para 1.208, p 53

404 Q433

405 Q435

406 Q433

407 HMRC, [Taking Control of Goods](#), April 2014, p 1

408 HMRC, [The county court – what it means for you](#), April 2012

409 HMRC, [Taking Control of Goods](#), April 2014, p 1

Banking Manual states that these “provisions are rarely used and such a warrant would be granted only in exceptional circumstances, depending on the quality of the evidence”.⁴¹⁰

230. If HMRC is unable to recover the outstanding tax by distraint, it can begin:

- Magistrates court proceedings; and
- County court proceedings.⁴¹¹

Before HMRC can begin any debt recovery proceedings, the taxpayer can appeal HMRC’s decision. The taxpayer can ask for the case to be either reviewed by HMRC and/or heard by an independent tribunal. To do so the taxpayer must send their appeal to HMRC in writing, within 30 days of the date of the initial HMRC correspondence. Once the appeal is submitted to HMRC, a taxpayer can apply to postpone paying the amount of tax under dispute. Interest will still accrue on the postponed amount until the appeal is resolved and any unpaid tax is paid.⁴¹²

231. The majority of appeals will be settled by agreement with HMRC. However, where an agreement cannot be reached, the taxpayer can request a review of HMRC’s decision by another HMRC officer not previously involved in the original decision. If the disagreement is still not resolved the taxpayer can appeal to the First-tier Tribunal. The taxpayer will have to request this appeal within 30 days of the review conclusion letter. The tax tribunal is independent of HMRC and will listen to both sides before reaching a decision. The tribunal can alter the decision if it thinks it is wrong. If the tribunal rules against the taxpayer, further appeals are only permitted if legal mistakes have been made during the case.⁴¹³

232. Each of the three professional bodies who submitted evidence to the Committee raised serious concerns about HMRC’s new debt recovery powers. The Institute of Chartered Accountants in England and Wales (ICAEW) said that these new powers are “extremely worrying and excessive” and “adequate safeguards are essential”.⁴¹⁴ The Chartered Institute of Taxation (CIOT) said:

We have strong concerns about the announcement that HMRC will have the power to take money directly from the bank accounts of tax debtors who owe more than £1,000 in tax or tax credits. This power is unprecedented in the UK and the announcement contained no details of any judicial or other safeguards that would protect taxpayers on low incomes struggling with debt problems—apart from a stipulation that a minimum of £5,000 would be left in debtors’ accounts.⁴¹⁵

233. A number of witnesses expressed concerns that the new debt recovery powers would mean that HMRC would be able to determine which taxpayers owed money and how

410 HMRC website, *Debt Management and Banking Manual: Enforcement action: distraint: carrying out a distraint: right of entry*

411 HMRC website, [What could happen if you don't pay HMRC](#)

412 HMRC website, [How to appeal against an HMRC decision - direct tax](#)

413 GOV.UK, *Tax tribunal: If you lose your case*

414 ICAEW, [written evidence](#)

415 CIOT, [written evidence](#)

much they owed, and then enforce that decision without any independent oversight. Mr Haskew said:

[...] we cannot have HMRC acting as judge and jury. There must be an element of oversight, and I think our preference is some sort of judicial oversight, possibly by way of a tribunal.⁴¹⁶

Mr Stevens agreed:

The real point is whether there will be a necessity to go to an external court—someone outside HMRC. That for me is the big question. If the whole thing takes place within the tax administration it leaves more cause for anxiety than otherwise.⁴¹⁷

234. In its written evidence to the Committee, CIOT said that without adequate safeguards or recourse to the courts, the impact of the policy could be serious for low-income earners:

People who owe HMRC £1,000 or just over may simply be people on low incomes or low wages who have come into difficulties and are in debt not only to HMRC but also to others, notably public utilities. To let HMRC raid their bank accounts [...] would be to flout the rule of law in a manner unworthy of a public service body. It is not the same as seizing physical goods, it is depriving the debtor of the very means to live.⁴¹⁸

235. Another concern raised by CIOT was that this new proposed power could “undermine confidence in the relationship between taxpayers and HMRC and actually discourage compliant behaviour”.⁴¹⁹ The ICAEW explained that HMRC’s new powers could create “perverse effects” such as increasing the amount of money held outside banks and building societies in order to avoid it being seized by HMRC.⁴²⁰

236. Under Crown preference, which originated in the late 19th century, liquidators were bound by statute to give preferential status to debts due to the Inland Revenue and HM Customs & Excise before any payment was made to other unsecured creditors.⁴²¹ After a consultation period, the Government decided to abolish Crown preference with the introduction of the Enterprise Bill in March 2002. It said that “in recent years the trend in other jurisdictions has been towards restricting or abolishing Crown or State preference” and that this was “more equitable”.⁴²² In its written evidence to the Committee, the ICAEW was concerned that the proposed new debt recovery powers for HMRC represented a return to Crown preference. It told us that “HMRC is effectively to become a preferential creditor under these new rules”.⁴²³

416 Q513

417 Q510

418 CIOT, [written evidence](#)

419 CIOT, [written evidence](#)

420 ICAEW, Finance Bill Briefing, April 2014

421 Department for Trade and Industry, [Productivity and Enterprise: Insolvency – A Second Chance](#), para 2.19, p 12

422 Department for Trade and Industry, [Productivity and Enterprise: Insolvency – A Second Chance](#), para 2.19, p 12

423 ICAEW, [written evidence](#)

237. Mr Stevens told the Committee that, regardless of the number of safeguards put in place surrounding HMRC's ability to directly access bank accounts, the policy "does rely on the authority having worked out how much money should correctly be taken from it in the first place".⁴²⁴ Both the ICAEW and CIOT raised concerns about the announcement in the Red Book that HMRC would only recover assets from the bank accounts of debtors who had the "financial means to pay".⁴²⁵ They were concerned about how HMRC would be able to determine who had the financial means to pay and under what criteria it would be judged. In addition, the ICAEW questioned how up-to-date HMRC's databases were and said that there had been "numerous cases recently of HMRC chasing debts which are not due, including attempting to confiscate assets".⁴²⁶ Mr Haskew gave some examples of the sorts of errors HMRC had been making:

One of our members recently had a letter from HMRC threatening distraint on his assets because he had not paid a tax liability, and the letter he got said his tax liability was nought. HMRC was chasing someone and threatening distraint on a tax that was ostensibly due of nothing.

[...]

Another last week was an employer who was being threatened with a collector coming round to collect assets to cover the debt. The debt had been paid in full in January, and this was the end of March.⁴²⁷

238. HMRC has, in the past, committed errors on a much larger scale. For example, in 2007, HMRC lost two computer discs containing Child Benefit data which included the name, address, date of birth, National Insurance number and, where relevant, bank details of 25 million people.⁴²⁸

239. The Chancellor told us that the power for HMRC to take money from people's accounts would not be unique to the UK. He said that "The DWP already have this power [to take money directly from bank accounts] with child maintenance payments".⁴²⁹ The Child Maintenance and Other Payments Act 2008, amending the Child Support Act 1991, provided the following power to the Child Maintenance and Enforcement Commission:

Orders for regular deductions from accounts.

(1) If in relation to any person it appears to the Commission—

- (a) that the person has failed to pay an amount of child support maintenance; and
- (b) that the person holds an account with a deposit-taker;

424 Q509

425 HM Treasury, [Budget 2014](#), 19 March 2014, para 1.208, p 53

426 ICAEW, [written evidence](#)

427 Q511

428 BBC, [UK's families put on fraud alert](#), 20 November 2007

429 Q434

it may make an order against that person to secure the payment of any amount due under the maintenance calculation in question by means of regular deductions from the account.⁴³⁰

On 1 August 2012, following the abolition of the Child Maintenance and Enforcement Commission, these powers were given to the Secretary of State.⁴³¹

240. Child maintenance is not, however, a payment from or to the state. The Department for Work and Pensions, through the Child Maintenance Service, acts as an intermediary between parents, rather than on its own account. As Child Maintenance Options, a service provided by the Child Maintenance Group, which is part of the Department for Work and Pensions, explains:

Child maintenance isn't a benefit that separated parents can "claim" from the state. It's paid by the other parent, and is a way of making sure both parents contribute to their child's upkeep when they live apart. When a family-based arrangement isn't possible, the state will get involved—but only to collect and pass on payments.⁴³²

The Chancellor told us that the form of debt recovery he proposed for HMRC is carried out in Sweden, Denmark, Ireland, Finland and New Zealand. The Red Book tells us that France and the US also have these powers.⁴³³

241. In the US, the Internal Revenue Service (IRS) can seize "all property and rights to property"⁴³⁴ of a taxpayer who owes Federal tax.⁴³⁵ However, specific actions must be completed before the seizure of a taxpayer's assets can be recommended:

- The liability must be verified;
- Alternative collection methods must be thoroughly considered;
- An analysis must be conducted to show that the expenses expected to be incurred with respect to the seizure do not exceed the fair market value of the asset to be seized;
- There must be a determination that the equity is sufficient to yield net proceeds from the sale to apply to the liability.⁴³⁶

The IRS cannot recover the outstanding tax from a person's bank account if it would result in economic hardship for the taxpayer. Economic hardship is defined as an individual being unable to pay their reasonable necessary living expenses.⁴³⁷ The determination of a

430 Child Maintenance and Other Payments Act 2008, section 22

431 The Public Bodies (Child Maintenance and Enforcement Commission: Abolition and Transfer of Functions) Order 2012, Section 34

432 <http://www.cmoptions.org/en/maintenance/index.asp>, What is Child Maintenance?, accessed 9/4/14

433 HM Treasury, [Budget 2014](#), 19 March 2014, para 1.208, p 53

434 Rights to property include income, bank accounts and social security payments.

435 Internal Revenue Service, [Internal Revenue Manual, Part 5, Chapter 17, Section 3, Property and Rights to Property](#)

436 Internal Revenue Service, [Internal Revenue Manual, Part 5, Chapter 10, Section 1, Actions Required Prior to Seizure](#)

437 Internal Revenue Service, [Internal Revenue Manual, Part 5, Chapter 11, Section 2, Economic Hardship](#)

‘reasonable amount for basic living expenses’ will vary according to the unique circumstances of the individual taxpayer.

242. Following the merger of HM Customs and Excise and the Inland Revenue in April 2005, an extensive review of HMRC’s powers, deterrents and safeguards was carried out. This review ran from 2005 to 2012 and its aim was to consider the scope for aligning and rationalising powers to make it easier for individuals and businesses to comply with their tax obligations and receive the tax credits to which they are entitled.⁴³⁸ In its June 2007 consultation paper entitled *Payments, Repayments and Debt: The Developing Programme of Work*, HMRC proposed extending its powers so that bank accounts could be accessed in order to settle outstanding tax debts, without the need for an application to the court.⁴³⁹ The consultation response document said that this proposal “attracted the largest number of responses, with 69 of the 95 written responses including a comment.”⁴⁴⁰ The most commonly raised concerns were that:

HMRC would have insufficient safeguards for this to be implemented appropriately and that it could create hardship. The level of HMRC error was a major point that would need to be addressed before any such scheme could be implemented. There was doubt over current customer service levels and that HMRC would be unable to support the system if it were introduced.⁴⁴¹

A small number of respondents suggested that this proposal would be a “draconian measure and that HMRC should not be given these powers under any circumstances”.⁴⁴² Following the strong opposition at the time, HMRC decided against taking the proposal further.⁴⁴³

243. On 6 May HMRC issued a consultation document, *Direct Recovery of Debt*.⁴⁴⁴ The closing date for the consultation is 29 July 2014. The document discusses the processes and safeguards that HMRC proposes for the new debt recovery powers the Chancellor announced. We have not had time to examine the document in any detail, but it appears to have been produced in haste.

244. The proposal to grant HMRC the power to recover money directly from taxpayers’ bank accounts is of considerable concern to the Committee. It could develop into a return to Crown preference by stealth. The Committee considers a lengthy and full consultation to be essential. The greater detail provided by the Government on 6 May will need further and extensive examination, and the Committee will take further evidence on this. Giving HMRC this power without some form of prior independent

⁴³⁸ HMRC, [HM Revenue and Customs and the Taxpayer: Modernising Powers, Deterrents and Safeguards](#), March 2005, p 2

⁴³⁹ HMRC, [Payments, Repayments and Debt: The Developing Programme of Work](#), Consultation Document, 25 June 2007, para 5.12, p 21

⁴⁴⁰ HMRC, [Payments, Repayments and Debt: Responses to Consultation and Proposals](#), 10 January 2008, para A6.2, p 15

⁴⁴¹ HMRC, [Payments, Repayments and Debt: Responses to Consultation and Proposals](#), 10 January 2008, para A6.2, p 15

⁴⁴² HMRC, [Payments, Repayments and Debt: Responses to Consultation and Proposals](#), 10 January 2008, para A6.3, p 15

⁴⁴³ HMRC, [Payments, Repayments and Debt: The Next Stage](#), November 2008, para 5.41, p 27

⁴⁴⁴ HMRC, [Direct recovery of debts](#), 6 May 2014

oversight—for example by a new ombudsman or tribunal, or through the courts—would be wholly unacceptable.

245. The Chancellor argues that this measure can be justified because the Department for Work and Pensions already has the right to take money directly from people's bank accounts to pay child maintenance. However, the parallel is not exact: in those cases, DWP is acting as an intermediary between two individuals. HMRC would be acting not as an intermediary between two individuals but rather in pursuit of its own objective of bringing in revenue for the Exchequer.

246. This policy is highly dependent on HMRC's ability accurately to determine which taxpayers owe money and what amounts they owe, an ability not always demonstrated in the past. Incorrectly collecting money will result in serious detriment to taxpayers. The Government must consider safeguards, in addition to those set out in the consultation document, to ensure that HMRC cannot act erroneously with impunity. These might include the award of damages in addition to compensation, and disciplinary action in cases of abuse of the power.

247. The ability directly to have access to millions of taxpayers' bank accounts raises concerns about the risk of fraud and error, and this should also be covered by the consultation.

248. Following the merger of HM Customs and Excise and the Inland Revenue in April 2005, an extensive review of HMRC's powers, deterrents and safeguards was carried out from 2005 to 2012. The Committee believes that sufficient time has now passed to warrant a post-implementation review of these powers. The aim of this review should be to ensure that all the powers HMRC has at its disposal remain relevant and are no more than are sufficient to enable HMRC to achieve its objectives.

Savings rate of income tax

249. At present, an individual whose only taxable income is savings income is entitled to have the first £2,790 of income above his or her Personal Allowance taxed at 10 per cent, rather than the 20 per cent rate at which non-savings income would be taxed. Savings income above this £2,790 threshold is taxed at the 20 per cent basic rate, the 40 per cent higher rate or the 45 per cent additional rate, depending on the person's total income. For an individual with a mix of savings and non-savings income whose earnings are less than the Personal Allowance plus £2,790, some or all of his or her savings income will be taxable at 10 per cent.

250. The Chancellor announced in his Budget statement that, from April 2015, the 10 per cent rate of savings income tax will be reduced to 0 per cent. In addition, the band of savings income to which this rate applies will be increased from £2,790 to £5,000. When combined with the increase to the Personal Allowance (to £10,500), the effect of this change is that anyone with total income of less than £15,500 per annum will no longer pay any tax on their savings income.

251. These changes were broadly welcomed by those who commented on them. The Chartered Institute of Taxation said that the announcement was “great news for prudent savers on modest incomes.”⁴⁴⁵ The Chairman of the Low Incomes Tax Reform Group, Anthony Thomas, said: “This relief should help add value to people’s money, particularly for those nearing the end of their working life, thus helping both pensioners and those entering retirement.”⁴⁴⁶

252. There were concerns, however, that the benefits of the change could be reduced because of the administrative complexities of the savings rate. Those eligible to pay no tax on their savings can fill in an R85 form (*Getting your interest without tax taken off*) to instruct their bank or building society to pay their interest gross. Those who find that they have overpaid tax on their savings income can reclaim it by completing an R40 form (*Claim for repayment of tax deducted from savings and investments*). Before the Budget, the Building Societies Association called on the Government to simplify this existing system, saying:

The tax system makes it unnecessarily difficult for savers who pay little or no income tax to register their savings accounts to receive interest gross—each account requires a separate R85 form. Similarly the mechanism for a saver eligible for the 10p savings tax is complex and is neither well known nor understood by the public. Both of these could be simplified.⁴⁴⁷

253. After the Budget, the Institute for Fiscal Studies suggested that “incomplete take-up” would be “a major challenge” for the Government in implementing the 0 per cent rate of savings income tax.⁴⁴⁸ In a press release, the Low Income Tax Reform Group said:

[...] people will only complete R85 if they know about it and understand that they are eligible. As LITRG have noted in a report published last year, this is often not the case. The onus is now on banks and building societies and HMRC to ensure that the R85 system is better publicised—now more than ever if today’s changes are going to have the desired impact on savers’ pockets.⁴⁴⁹

254. The Committee welcomes the Government’s decision to reduce the starting rate of savings income tax to 0 per cent and to increase to £5,000 the band of savings income to which this rate applies. There is, however, a risk that the benefits of this measure could be eroded if those who are eligible for the 0 per cent rate do not understand that they are eligible or do not know which forms they need to complete. We urge HMRC to set out a clear plan describing how it will work and how banks and building societies will ensure that relevant savers are aware of this change.

445 Chartered Institute of Taxation, [written evidence](#)

446 “[0% rate will add value to the savings of those on modest incomes](#)”, Low Incomes Tax Reform Group press release, 19 March 2014

447 Building Societies Association, [BSA calls for a Budget for savers](#), Press release, 4 March 2014

448 Institute for Fiscal Studies, [Budget 2014: pensions and savings policies](#), Carl Emmerson, 20 March 2014, Slide 4

449 “[0% rate will add value to the savings of those on modest incomes](#)”, Low Incomes Tax Reform Group press release, 19 March 2014

Annual Investment Allowance

255. The Government announced in the Red Book that the Annual Investment Allowance (AIA) will be doubled to £500,000 from April 2014 to December 2015,⁴⁵⁰ with the aim of benefiting small and medium sized firms. Andrew Courts, Member of ACCA Global Tax Forum, told the Committee that the AIA was “great for small businesses” but raising the allowance from £250,000 to £500,000 would not benefit many small and micro businesses. He said that the original £250,000 was “adequate for most small businesses”.⁴⁵¹

256. Similar concerns were expressed by the Chartered Institute of Taxation:

[...] we believe that [the increase in the AIA] will have a limited impact on small and medium-sized enterprises (SMEs). The Chancellor said in his speech that this measure will mean that 99.8% of businesses will receive 100% up-front relief on their qualifying investment in plant and machinery. We note that when the Chancellor previously announced the reduction of the limit from £100,000 to £25,000 with effect from April 2012, the Government indicated that the reduction would not impact 95% of businesses. Taking the two announcements together suggests that rather less than 5% of all businesses will benefit from the temporary doubling.⁴⁵²

257. A number of witnesses raised concerns about the stability and certainty of the AIA. Our report on the *Principles of Tax Policy* outlined the importance of these principles:

Tax policy is only one of the factors on which businesses and individuals make their decisions, but lack of stability and clarity about the direction of travel in tax policy will, over time, undermine the competitiveness of a tax system and make it impossible for businesses to plan. If tax policy is to support growth, then the direction of travel of tax policy should be clear.⁴⁵³

The Association of Chartered Certified Accountants (ACCA) highlighted that the AIA has been changed four times in the last five years:⁴⁵⁴

AIA allowance changes

Table 7: AIA allowance changes

	From April 2008 to April 2010	From April 2010	From April 2012	From January 2013	From April 2014 until December 2015
Annual Investment Allowance	£50,000	£100,000	£25,000	£250,000	£500,000

Source: HMRC website

450 HM Treasury, [Budget 2014](#), 19 March 2014, para 1.102, p 31

451 Q533

452 Chartered Institute of Taxation, [written evidence](#)

453 Treasury Committee, Eighth Report of Session 2010–12, [Principles of Tax Policy](#), HC 753, para 60, p 21

454 ACCA, [written evidence](#)

258. Mr Stevens told the Committee that “the constant change and moving around leads to uncertainty”⁴⁵⁵ and that this uncertainty “genuinely does discourage business from doing things.”⁴⁵⁶ The Confederation of British Industry (CBI) welcomed the extension and enhancement of the AIA, saying that “this will provide a shot in the arm for all businesses, but will particularly support investment by SMEs.”⁴⁵⁷ However, they stressed the importance of making the increase in the allowance permanent:

[...] making the enhanced Annual Investment Allowance permanent at a higher threshold of at least £250,000 would provide a longer term solution to correcting the UK’s comparatively uncompetitive capital allowances regime.

[...]

Even under current plans, the Allowance is due to be drastically reduced to £25,000 in 2016.⁴⁵⁸

The Chartered Institute of Taxation (CIOT) had a similar view in that setting the AIA at a “sensible level—such as £100,000—for the long-term would have done far more to promote business confidence than another temporary increase”.⁴⁵⁹

259. The more complex a tax system is, the harder it is to administer and the harder it is for taxpayers to assess their own liability.⁴⁶⁰ Mr Steven told the Committee that the volatility in the AIA has resulted in the most “complicated set of calculations I had seen for quite some time”.⁴⁶¹ Mr Courts agreed:

Clients will see the [Annual Investment Allowance] headline on the news and then have to ask how it relates to them. Before we can give them a straight answer, we have to sit down and work out their year-end, what they are going to spend, and follow it all the way through. So when it went from £50,000 to £25,000 to £250,000, in one year they could have three different rates of allowance and they are not going to get just one figure. The rate of allowance that they would get would also depend on when they purchased the item. That meant that there was quite a lot of uncertainty during that period.⁴⁶²

260. The frequency of changes to the annual investment allowance over the past seven years has created uncertainty and instability for businesses and imposed an economic cost. The Committee has previously highlighted the importance of stability in the tax system in its 2011 Report, *Principles of Tax Policy*. We therefore recommend that the Treasury develop a strategy for future annual investment allowance changes to reduce the current instability and help business planning.

455 Q534

456 Q534

457 CBI, written evidence

458 CBI, written evidence

459 Chartered Institute of Taxation, [written evidence](#)

460 Treasury Committee, Eighth Report of Session 2010–12, [Principles of Tax Policy](#), HC 753, p 28

461 Q534

462 Q535

6 Parliamentary timing

261. It was until recently the practice of the Treasury Committee to report to the House on the Budget in time for the Second Reading of the Finance Bill. The timetabling of the Finance Bill in recent years has meant that this was last possible in 2011. In 2012, we were able to publish our report in time for the beginning of the Committee stage of the Finance Bill on the floor of the House.

262. This year—as in 2013—the timings of the Budget and the Finance Bill have prevented us from publishing our report before Committee stage. The Chancellor made his Budget statement on 19 March, the Finance Bill was published on 27 March, and Second Reading took place on 1 April. Committee of the Whole House began on 8 April—less than three weeks after the Budget.

263. We accept that there is some urgency to passing the Finance Bill. The Provisional Collection of Taxes Act 1968, as amended by the Finance Act 2011, provides that a Budget resolution expires seven months after the date on which it was to take effect, or, if no date is specified, seven months after the date on which the resolution was passed. In practice, this means that the Finance Bill should have completed its passage through Parliament before the summer recess. This is a tight timetable. The Commons Public Bill Committee stage does not, by convention, start until the Committee of the Whole House stage has ended. Once the Public Bill Committee stage has ended, there needs to be time for the Bill to be reprinted before the two days allotted to Report stage and Third Reading. There is then the customary two weekends before consideration of the Bill can begin in the House of Lords.

264. In 2012, we noted that the then new pattern of Prorogation and State Opening risked making the timing of the stages of future Finance Bills even tighter, because it reduced the amount of sitting time available before the summer recess. In its response to our Report on the 2013 Budget, the Government acknowledged that this risk had materialised:

The Government recognises that the interval between publication of the Finance Bill and Second Reading, and between Second Reading and Committee of the Whole House, has been shorter than in the recent past. However, as the Committee has itself noted, this is largely a consequence of the new pattern of Prorogation and State Opening of Parliament.⁴⁶³

265. In 2012, we concluded that the timings of the Second Reading and the Committee of the Whole House stage of the Finance Bill had been “wholly unsatisfactory” and therefore recommended that:

[...] the Treasury and the Business Managers work together to plan the timings of future Budgets and Finance Bills so that the House has longer between publication of the Bill and Second Reading and, particularly, between Second Reading and

⁴⁶³ Treasury Committee, Second Special Report of Session 2013–14, Budget 2013: Government and Office for Budget Responsibility Responses to the Committee's Ninth Report of Session 2012–13, HC 370, para 17

Committee of the Whole House. This may require the Budget to be somewhat earlier in future.⁴⁶⁴

266. In 2013, the Second Reading of the Finance Bill was on a Monday, with Committee of the Whole House on Wednesday and Thursday of the same week. In our Report on the 2013 Budget, we reiterated the recommendation we had made in 2012, and further recommended that “there should be at least a weekend between Second Reading and the beginning of Committee of the Whole House”.⁴⁶⁵

267. We welcome the fact that this year, in accordance with our recommendation, there was a full sitting week between Second Reading and Committee of the Whole House. On the other hand, the time allowed between the Budget and Second Reading—less than two weeks—and between publication of the Finance Bill and Second Reading—only one full sitting day—was wholly inadequate.

268. The time available for this Committee to conduct an inquiry into the Budget, and for outside experts to consider its effects in detail, will always be limited. The Treasury Committee does, however, need adequate time to take written and oral evidence from expert witnesses and to prepare and publish a report.

269. Between 2003 and 2011, it was customary for more than four weeks to elapse between the Budget and Second Reading of the Finance Bill. In our Report on the 2002 Budget, we noted that the period between the Budget and the Finance Bill had, until then, been “typically in the range of four to six weeks”.⁴⁶⁶ Even allowing for the sitting time lost under the new pattern of parliamentary Sessions, it should be possible for the Government to allow three sitting weeks for scrutiny between the Budget and the Second Reading of the Finance Bill. It would also be open to the Government to produce the Budget slightly earlier, to allow more time for scrutiny.

270. It is essential that the Budget and the Finance Bill receive adequate, detailed parliamentary scrutiny. Prior to 2011, it was customary for four to six weeks to elapse between the Budget and the Second Reading of the Finance Bill. In the most recent three years, this has fallen to an average of just under three weeks. We welcome the Government’s provision of a full sitting week between Second Reading and Committee of the Whole House. Nevertheless, this year, the timings of the Budget and the Finance Bill have not permitted adequate scrutiny to take place—either by this Committee or outside—in time for either Second Reading or Committee of the Whole House. We therefore recommend that, in future, there should be no less than three sitting weeks between the Budget and Second Reading of the Finance Bill, and at least a further sitting week between Second Reading and Committee of the Whole House. Four to six weeks between the Budget and Second Reading of the Finance Bill was once the norm, so our proposal will simply bring the arrangements closer to the practice that pertained before 2011. We accept that it may not be possible to achieve this timetable in an election year, but it certainly should be the accepted practice at other times.

464 Treasury Committee, Thirtieth Report of Session 2010–12, *Budget 2012*, [HC 1910](#), para 2

465 Treasury Committee, Ninth Report of Session 2012–13, *Budget 2013*, [HC 1063](#), para 211

466 Treasury Committee, Second Report of Session 2001–02, *2002 Budget*, [HC 780](#), para 1

Conclusions and recommendations

Introduction

1. It is regrettable that the Government did not supply details of its additional support for childcare to the OBR in time for it to verify the Government's claims about the costs of this policy. The OBR has said that it will look at this measure closely in the run up to the Autumn Statement. It is not acceptable, however, that the Government's figures should be left unverified for what may be more than eight months. We recommend that, when Budget announcements are not submitted before the OBR's deadline, the OBR should scrutinise major uncosted policies as soon as reasonably possible thereafter and publish its findings. (Paragraph 7)
2. We welcome the fact that the Government maintained the confidentiality of the Budget this year. This can only have helped the presentation of the Budget measures. This Budget was unusual, however, in that one of its most important components—the reform of pensions—was highly market sensitive: the rules against selectively disclosing market sensitive information appear to have constituted a powerful enough deterrent to advance briefing of those reforms. We will expect this year's good practice in maintaining confidentiality to be maintained in future Budgets, when such considerations do not necessarily apply. (Paragraph 10)

Macroeconomy

3. House price and commercial real estate bubbles are easy to spot in retrospect. The problem for the Financial Policy Committee is to spot them in advance of their bursting and take whatever action is required to mitigate their negative effects on financial stability. (Paragraph 54)
4. Wider economic concerns are the responsibility of the Government and the Monetary Policy Committee. The Government is also responsible for fiscal and policy tools which directly influence the housing market. It should therefore state what indicators it believes are most important in detecting any wider economic risks arising from the housing market. It should also set out how it plans to address these risks, should they arise. (Paragraph 55)
5. The Chancellor has asked the FPC to be “particularly vigilant against the emergence of potential risks in the housing market”. It is not clear precisely what this means in practice, since the new remit document endorses the existing levels of vigilance. The Chancellor should provide a more detailed explanation of his comment, and whether he expects the FPC to interpret its remit in a way that might prompt it to take further action as a consequence. (Paragraph 56)
6. The evidence we took concurred with the view of the OBR that the recovery to date has been driven by an increase in demand without a corresponding rise in supply potential. The output gap is being reduced in size and, so far, there is insufficient evidence to support the view that productivity growth is returning. (Paragraph 65)

The public finances

7. For the fourth Economic and Fiscal Outlook in a row, the OBR forecasts that the Government will meet the rolling fiscal mandate, but not the supplementary target. In line with previous occasions, the Government has not proposed any corrective action in order to meet the supplementary target. Instead the Government has allowed the automatic stabilisers to continue their work, rather than taking corrective action—tightening fiscal policy—in order to meet the supplementary target. (Paragraph 70)
8. The Budget was fiscally neutral on a five year view—the forecast period. Four of the measures announced have consequences within the forecast period that differ significantly from their longer term effects. These measures are fiscally positive within the five year forecast period. However, this tapers and they are projected to be fiscally negative after 20 years. While the effect of these four spending decisions may be small, and subject to uncertainty, the Committee would be concerned if the Government made fiscal decisions with its eye only on the five year forecast period. It is important that the OBR cost the long term implications of Budget measures. (Paragraph 78)
9. After an economic shock, cyclically adjusted measurements are particularly uncertain. The current fiscal mandate is dependent on an unobservable output gap. It has been made even more unreliable as a consequence of the financial crisis. (Paragraph 83)
10. For most of the last 30 years, governments have been trying to devise a robust fiscal anchor. There have been successive Medium Term Financial Strategies; the Code for Fiscal Stability (modified during the crisis by the temporary operating rule); and the Charter for Budget Responsibility. The Government is now considering a new Charter for Budget Responsibility. Fiscal anchors have merit. But at a time when the credibility of pledges in all aspects of public policy has attracted greater scepticism than before, it will be more difficult to build confidence in the fiscal anchor deep enough to withstand an extreme event. (Paragraph 84)
11. Ring fencing distorts spending decisions. It also weakens rigorous scrutiny of spending in ring fenced departments. Furthermore, with each year that ring fencing remains in place, the size of ring fenced departments increases as a proportion of total departmental spending. The IFS has stated that by 2015-16, expenditure reductions of 21 per cent will have been implemented in areas other than the NHS, schools and overseas aid. Each successive round, seeking reductions from an already smaller non-ringfenced base, will be more difficult than its predecessor. (Paragraph 89)
12. 17 per cent of headline total managed expenditure in 2012-13 would have been covered by the welfare cap. The cap raises a number of concerns and we intend to seek further written evidence on its design and operation. Some welfare spending is not included within the cap. This may distort decision making, for example by tempting a government to change welfare entitlements in order to avoid breaching it. The penalty for a breach of the cap is any political embarrassment that may come with Parliamentary debate, a requirement in the event of its breach. The cap is

therefore declaratory. Previous examples of such declarations include the child poverty target and the fuel poverty target. (Paragraph 105)

Pension reforms and savings

13. The Committee notes that all witnesses welcomed the greater flexibility and choice provided by the Government's proposed pension reforms. We further note the Chancellor's commitment to "free, impartial, face-to-face advice", which will be important for many people for the reforms to work. (Paragraph 118)
14. The full impact of the pension reforms on the long-term social care budget remains uncertain. The Government is right to require the long-term care means test to be revised in the light of these reforms. The Government has an understandable desire to have the radical changes to pensions completed as soon as possible. Because the reforms both to pensions and to long-term care come into force simultaneously, the revision of the long-term care means test should be completed in time for those who may be affected by both these reforms to make informed choices. (Paragraph 132)
15. Until now there have been very strong incentives to purchase an annuity at the point of retirement. Creating greater freedom and choice in retirement will require individual consumers to consider the range of circumstances they may face, in particular relating to longevity. They will need to make informed decisions based on their personal needs and likely circumstances. For some consumers, these choices will require substantial guidance. (Paragraph 136)
16. The market is likely to adapt, offering a new range of financial products for those approaching retirement. It is crucial that these products are not defective. Were they to be so, the reputation of the financial services industry, which has suffered severe damage in recent years from large scale mis-selling, would be further tarnished. (Paragraph 144)
17. The FCA has now been given new powers to intervene early, in advance of detriment occurring. In practice, this will be extremely difficult to accomplish without creating other forms of consumer detriment. In particular, it will be essential to avoid stifling market innovation. The use of these new powers will be a major test of judgement-based regulation. (Paragraph 145)
18. The impact of these reforms on the annuity market will only be known after a number of years. Increased flexibility and choice in retirement will only benefit consumers if an active and innovative market offers a range of products, which should include annuities, to suit individual requirements. (Paragraph 152)
19. There is a clear distinction in financial services between regulated advice and guidance. Although what was proposed was clear in the Budget Red Book and in the consultation document, the Chancellor's Budget statement on this point could have been better phrased. (Paragraph 161)
20. The guidance made available to consumers must explain what, if any, protection they may have in cases of poor guidance. (Paragraph 162)

21. The guaranteed guidance must be available to people well in advance of their retirement to help their decision-making. (Paragraph 165)
22. Given that the Money Advice Service has been asked by the Treasury to play a role in developing the standards for financial guidance at retirement, it is even more important that the independent review of the MAS is completed quickly. (Paragraph 168)
23. It is essential for the success of the pensions reforms that the guidance offered under the guidance guarantee is trusted by those who use it. The guidance offered under the guarantee must therefore be demonstrably impartial. It must certainly not be biased in favour of any particular product type or provider. (Paragraph 170)
24. It will be important for the success of this policy that people receive high quality guidance. As well as being of value to the individual it will have public policy benefits. People need to be aware that while the guidance is to be free at the point of use, the costs of firms providing it will be borne by consumers. It is crucial that people grasp the value of this guidance. We therefore recommend that the full average cost of the provision of the guidance by firms be estimated and disclosed to consumers. (Paragraph 173)
25. The 'guidance guarantee' is not the only Government sponsored guidance being designed for pensioners or those who are approaching retirement. These schemes should operate in concert to help people make informed decisions about what is right for them in retirement. (Paragraph 178)
26. The Chancellor's commitment was for face-to-face advice to be available. Evidence to the Committee from a number of witnesses suggested a desire to use other channels. These will be appropriate for some customers but, in line with the Government's pledge, it is important that at least for those who choose face-to-face guidance this is provided without financial detriment to the customer. (Paragraph 185)
27. The pension reforms announced by the Government are welcome, and also transformational. Consumers will need considerable support in navigating a market which is undergoing major change and in which consumers are likely to be offered an array of new products. The Committee recommends that the proposed guidance under the guarantee observe the following principles. It should:
 - Be demonstrably impartial as to providers and type of product;
 - Include at least an initial opportunity for face-to-face guidance;
 - Be free at the point of use, with the costs of such provision made transparent;
 - Make clear to every consumer exactly what is being offered, the limitations of the guidance, and what protection it gives consumers in the event of detriment;
 - Be offered from at least 12 months in advance of the consumer's stated retirement date; and

- Be co-ordinated with Government-sponsored guidance relating to long-term care.
28. There are risks to individuals and the wider economy if people decide to concentrate their savings in a single asset class such as residential property. Contrary to widespread perception, residential property can be a volatile asset class and prone to large falls in value. (Paragraph 195)
29. Taken together, the changes announced in the Budget to ISAs, as well as the reforms to the taxation of defined contribution pensions at retirement, amount to a substantial increase in the flexibility available to savers. As this flexibility increases, ISAs and pensions will become increasingly interchangeable in their effect. In the light of this, the Committee recommends that the Government set out comprehensively the approach it intends to take to taxation of all forms of saving. This should include an examination of the merits of moving further towards taxing savings once, the scope for bringing closer together the tax treatment of ISAs and pensions, and the appropriateness of the present arrangements for the pension tax free lump sum. (Paragraph 205)
30. The Government's announcement that National Savings and Investments (NS&I) will offer 'pensioner bonds' at a market-leading rate represents something of a departure from NS&I's usual approach. NS&I is required to balance the funding needs of the Government, its customers and the wider financial services sector. Pensioner bonds have tilted this balance—in this case at least—in favour of customers and away from the Government and the financial services sector. The Government must provide clarity about the framework within which NS&I is now operating. (Paragraph 211)
31. Since the Government has decided that it wants NS&I to give priority to customer interests, we recommend that NS&I consider once again offering index-linked savings certificates. (Paragraph 212)
32. The increase of NS&I's Net Financing Target from £2 billion, plus or minus £2 billion, in 2013–14 to £13 billion, again plus or minus £2 billion, in 2014–15 could have a significant effect on NS&I's market share. The Government must ensure that this does not destabilise the wider savings market by crowding out private savings providers. (Paragraph 213)

Taxation

33. Retrospective tax legislation conflicts with the principles of tax policy recommended by this Committee. In our Budget 2012 Report we recommended that the Government restrict the use of retrospection to wholly exceptional circumstances. Witnesses told us that the Government was not abiding by this recommendation. Furthermore, the Red Book announced an additional retrospective taxation policy: an extension of the requirement for taxpayers to pay upfront any disputed tax associated with anti-avoidance schemes. This policy will retrospectively apply to some of the 65,000 outstanding tax avoidance cases. There may be a case for this policy but the Government has yet to explain what is wholly exceptional about these

cases that justifies this retrospective measure. It should do so in response to this Report. (Paragraph 225)

34. The proposal to grant HMRC the power to recover money directly from taxpayers' bank accounts is of considerable concern to the Committee. It could develop into a return to Crown preference by stealth. The Committee considers a lengthy and full consultation to be essential. The greater detail provided by the Government on 6 May will need further and extensive examination, and the Committee will take further evidence on this. Giving HMRC this power without some form of prior independent oversight—for example by a new ombudsman or tribunal, or through the courts—would be wholly unacceptable. (Paragraph 244)
35. The Chancellor argues that this measure can be justified because the Department for Work and Pensions already has the right to take money directly from people's bank accounts to pay child maintenance. However, the parallel is not exact: in those cases, DWP is acting as an intermediary between two individuals. HMRC would be acting not as an intermediary between two individuals but rather in pursuit of its own objective of bringing in revenue for the Exchequer. (Paragraph 245)
36. This policy is highly dependent on HMRC's ability accurately to determine which taxpayers owe money and what amounts they owe, an ability not always demonstrated in the past. Incorrectly collecting money will result in serious detriment to taxpayers. The Government must consider safeguards, in addition to those set out in the consultation document, to ensure that HMRC cannot act erroneously with impunity. These might include the award of damages in addition to compensation, and disciplinary action in cases of abuse of the power. (Paragraph 246)
37. The ability directly to have access to millions of taxpayers' bank accounts raises concerns about the risk of fraud and error, and this should also be covered by the consultation. (Paragraph 247)
38. Following the merger of HM Customs and Excise and the Inland Revenue in April 2005, an extensive review of HMRC's powers, deterrents and safeguards was carried out from 2005 to 2012. The Committee believes that sufficient time has now passed to warrant a post-implementation review of these powers. The aim of this review should be to ensure that all the powers HMRC has at its disposal remain relevant and are no more than are sufficient to enable HMRC to achieve its objectives. (Paragraph 248)
39. The Committee welcomes the Government's decision to reduce the starting rate of savings income tax to 0 per cent and to increase to £5,000 the band of savings income to which this rate applies. There is, however, a risk that the benefits of this measure could be eroded if those who are eligible for the 0 per cent rate do not understand that they are eligible or do not know which forms they need to complete. We urge HMRC to set out a clear plan describing how it will work and how banks and building societies will ensure that relevant savers are aware of this change. (Paragraph 254)

40. The frequency of changes to the annual investment allowance over the past seven years has created uncertainty and instability for businesses and imposed an economic cost. The Committee has previously highlighted the importance of stability in the tax system in its 2011 Report, Principles of Tax Policy. We therefore recommend that the Treasury develop a strategy for future annual investment allowance changes to reduce the current instability and help business planning. (Paragraph 260)

Parliamentary timing

41. It is essential that the Budget and the Finance Bill receive adequate, detailed parliamentary scrutiny. Prior to 2011, it was customary for four to six weeks to elapse between the Budget and the Second Reading of the Finance Bill. In the most recent three years, this has fallen to an average of just under three weeks. We welcome the Government's provision of a full sitting week between Second Reading and Committee of the Whole House. Nevertheless, this year, the timings of the Budget and the Finance Bill have not permitted adequate scrutiny to take place—either by this Committee or outside—in time for either Second Reading or Committee of the Whole House. We therefore recommend that, in future, there should be no less than three sitting weeks between the Budget and Second Reading of the Finance Bill, and at least a further sitting week between Second Reading and Committee of the Whole House. Four to six weeks between the Budget and Second Reading of the Finance Bill was once the norm, so our proposal will simply bring the arrangements closer to the practice that pertained before 2011. We accept that it may not be possible to achieve this timetable in an election year, but it certainly should be the accepted practice at other times. (Paragraph 270)

Appendix 1: Chartered Institute of Taxation

Principles of Tax Policy and Budget 2014

Introduction

The Treasury Committee has invited comments on how Budget 2014 (and succeeding Finance Bill) meets the Committee's tax policy principles, as expressed in its 2011 report on Principles of Tax Policy. The Chartered Institute of Taxation (CIOT) is pleased to submit some comments, which incorporate points relating to the unrepresented from our Low Incomes Tax Reform Group (LITRG) and also comments from our colleagues at the Association of Taxation Technicians (ATT).

The Committee's report identified six principles:

- Basic fairness;
- Supporting growth and encouraging competition;
- Certainty, including simplicity;
- Stability;
- Practicality; and
- Coherence.

We comment briefly under each of the principles but would stress that we are not giving a full analysis on the Budget/Finance Bill measure; indeed we cannot hope to cover the whole plethora of measures in the Budget in a short memorandum.

Basic fairness

As in previous years, much is made of the increase in the personal allowance taking people out of the tax net. However, if the objective is to improve the financial position of low-income households, increasing the income tax personal allowance is not the most efficient way of doing that, particularly while the NIC primary threshold remains at £7,956.

In general, higher rate taxpayers stand to gain more from any rise in the personal allowance than basic rate taxpayers, while non-taxpayers gain not at all. The position of low-income taxpayers who also claim benefits is complicated. To anyone on most means-tested benefits, any tax saving from the raising of the tax threshold will be offset by a diminution in their entitlement to benefit. This is because means-tested benefits are based on net, after-tax, income – accordingly any reduction in the tax bill results in an increase in net income, hence the reduction in benefit entitlement.

To illustrate, an increase in the personal allowance by, say, £1,000 will mean a 20% tax saving for a basic rate taxpayer - £200. But if that taxpayer is claiming Universal Credit,

their entitlement will be reduced by 65p for every £1 increase in their net income. So the actual saving for a taxpayer in this position is not £200, but 35% of £200, or £70.

We have strong concerns about the announcement that HMRC will have the power to take money directly from the bank accounts of tax debtors who owe more than £1,000 in tax or tax credits. This power is unprecedented in the UK and the announcement contained no details of any judicial or other safeguards that would protect taxpayers on low incomes struggling with debt problems – apart from a stipulation that a minimum of £5,000 would be left in debtors' accounts. We are concerned that the proposed power could undermine confidence in the relationship between taxpayers and HMRC and actually discourage compliant behaviour.

HMRC say they will use their new power only where debtors 'have the financial means to pay' and have been asked for payment many times. It is unclear how HMRC will determine whether a debtor has the financial means to pay, or by what criteria this will be judged. It is not uncommon for people in straitened financial circumstances to put insistent demands for payment on one side if they lack the means to pay, or to satisfy the most pressing debtor at the expense of others.

People who owe HMRC £1,000 or just over may simply be people on low incomes or low wages who have come into difficulties and are in debt not only to HMRC but also to others, notably public utilities. To let HMRC raid their bank accounts without safeguards or recourse to the courts – or with inadequate safeguards – would be to flout the rule of law in a manner unworthy of a public service body. It is not the same as seizing physical goods, it is depriving the debtor of the very means to live.

We understand there is to be a consultation on this measure. We sincerely hope the consultation document will reveal some coherent proposals on safeguards which are absent from the announcement itself.

There are some anti-avoidance measures that score well under the fairness heading. We would highlight the introduction of new powers for HMRC to tackle non-cooperative promoters of tax avoidance schemes. However, we are disappointed that the Government is to go ahead with proposals to demand that users of existing Disclosure of Tax Avoidance Schemes (DOTAS) pay the disputed tax in advance and without a right to appeal.

We understand and sympathise with the Government's need to strike down mass-marketed tax avoidance schemes, but allowing HMRC to act as prosecutor, judge and jury based on the DOTAS regime, which was not meant to be used for these purposes, is going too far. It is our opinion that this measure will weaken the DOTAS provisions and undermine confidence in the fairness of the UK tax system.

Supporting growth and encouraging competition

There are few positive measures for businesses in the Budget. However, we think that this is understandable given the steps taken in the last few years to improve the competitiveness of the UK tax system, not least the significant reduction in the main rate of corporation tax to 20% from 1 April 2015.

The headline announcement for businesses was the doubling of the Annual Investment Allowance (AIA) from £250,000 to £500,000. However, we believe that this will have a limited impact on small and medium-sized enterprises (SMEs). The Chancellor said in his speech that this measure will mean that 99.8% of businesses will receive 100% up-front relief on their qualifying investment in plant and machinery. We note that when the Chancellor previously announced the reduction of the limit from £100,000 to £25,000 with effect from April 2012, the Government indicated that the reduction would not impact 95% of businesses. Taking the two announcements together suggests that rather less than 5% of all businesses will benefit from the temporary doubling.

On a more positive note, the increase in the rate of the payable R&D tax credit for SMEs to 14.5% from 1 April 2014 will put more cash back in the hands of SMEs and encourage further investment in R&D. R&D tax relief is one of the most successful tax reliefs introduced in the UK, having supported almost £12 billion of R&D expenditure in 2011/12 alone, and the increase in the rate of the payable credit can only boost R&D activity in the UK.

We would highlight also the announcement that the Seed Enterprise Investment Scheme (SEIS) is to be made permanent. The SEIS was introduced in 2012 to help small, start-up companies raise equity finance. Investors can have confidence that the scheme will continue for the foreseeable future. This will increase investment in those small, high-risk companies identified as being key drivers of growth.

Certainty, including simplicity

As noted above, the Government is to go ahead with proposals to demand that users of DOTAS pay the disputed tax in advance. By applying the rules to existing schemes, this measure effectively has retrospective effect as it will apply to taxpayers who at the time they entered into the schemes would not have anticipated that they would have to make accelerated payments of the tax unless their case was eventually lost.

Taxpayers should be entitled to organise their affairs in accordance with the prevailing law in the certain knowledge that it may be changed in the future but that its impact cannot be backdated. Retrospective legislation creates doubt and uncertainty to the detriment of the economy at large. We believe that these proposals can only create uncertainty for taxpayers.

Certainty is essential if taxpayers are to be encouraged to contribute to pension schemes. While we welcome the changes made to pensions in the Budget, which we believe will bring increased flexibility for taxpayers, we note that since the fundamental reforms in Finance Act 2004, almost every subsequent Finance Act has made changes to the tax system around pensions. Further, we find it regrettable that some taxpayers, having made decisions based on the rules in place at that time, may now regret those decisions in light of the rules which are to apply in the future. We hope that Governments will resist the temptation to make further changes in this area, and so restore some degree of certainty to the tax rules around pensions.

We welcome the announcement that the Government will be implementing recommendations from the Office of Tax Simplification (OTS) that will significantly cut

administrative burdens for employers. Employers are subject to a cumbersome system for the reporting of employee benefits and expenses. Putting in place a system of voluntary payroll of benefits is long overdue and will cut down on end of year administration.

We think that the proposals on ISAs have the potential to enhance certainty and simplicity although much will depend on how the relevant provisions are framed. It will also depend on providers offering products that take full advantage of the new rules and not profiteering from high charges and low interest rates offered.

It was hoped that the legislation introducing the small transferable tax allowance for married couples and civil partners would have been crafted with simplicity in mind, given that the sort of taxpayers who will benefit from it the most will be on modest levels of income and unlikely to have professional representation. It is therefore unfortunate that the procedural burdens imposed by the legislation are extremely complex given the very small benefit to be derived and this complexity may well discourage take up of the relief.

We comment elsewhere in this submission on the proposed doubling of the AIA. If the relevant legislation is anything like that which was required to introduce the current temporary £250,000 limit, it will be arithmetically complex. The scheduled expiry date of 31 December 2015 for the enhanced limit (at which point the limit will in the absence of further proposals reduce from £500,000 to £25,000) does not make for certainty.

As a more general point, we continue to be concerned that taxpayers are taxed by statute and untaxed by HMRC guidance. In particular, we feel that this may be an issue with regard to the changes to the taxation of partnerships (which are considered in more detail below) where the legislation is possibly of wide application. HMRC have published guidance in this area which gives some comfort that the legislation will be applied in a reasonable manner. However, in our opinion this falls some way short of giving certainty to taxpayers.

Stability

Last year, we commented under this section on the changes to the AIA and to the tax system around pensions. It is testament to the volatility of these areas that they fall to be considered under this section again this year. The changes to the pension rules are clearly positive, but we have demonstrated above that the increase in the AIA will have little impact on businesses.

As a result of the changes made in this year's Budget, and previously, we have the illogical situation that depending on the precise date when a business incurs eligible capital expenditure over the next two years, the amount of that expenditure that it can immediately write off for tax purposes may in simple terms be £250,000, £500,000 or £25,000 (In fact there are many more permutations of amount depending on the accounting date of a business). Just getting the purchase date wrong by a single day could make a massive difference to the business's tax bill. We are always concerned when tax considerations get in the way of sound business decisions. Having a twenty-fold cliff-edge drop in the limit at midnight on 31 December 2015 could really distort decisions about capital expenditure.

It is regrettable that, despite the many changes made in this area, the position beyond 31 December 2015 is unclear. We think that it would be helpful for the SME sector if the Government indicated now what will happen after 31 December 2015. It is inconceivable that the limit will drop from £500,000 to £25,000 but that is how things will stand after Finance Act 2014 unless clarification is provided. If the Government sets out now what will happen from 1 January 2016, businesses will be able to plan sensibly. Setting the AIA at a sensible level – such as £100,000 – for the long-term would have done far more to promote business confidence than another temporary increase.

We would draw your attention also to the many changes announced in the Budget regarding the taxation of property, including: the immediate reduction in the threshold for the 15% SDLT rate from £2m to £500,000; the phased changes to the bands applying with regard to the Annual Tax on Enveloped Dwellings (ATED); and, as announced at the Autumn Statement, the proposed introduction of a charge to capital gains tax on future gains made by non-UK residents disposing of UK residential property. This is yet another round of changes to the UK's volatile property taxes regime, following on from the introduction of ATED and related changes to CGT and Stamp Duty Land Tax rates in recent years.

We would caution the Government not to over-react in its attempts to tackle abuse of Venture Capital Trusts (VCTs) and Enterprise Investment Schemes (EISs). Although we understand that this is part of a broader effort to crack down on tax avoidance, it is equally important to recognise that those schemes intended to increase investment in growing businesses must not be hampered by an over-zealous attempt to combat avoidance. It is a fine line between cracking down on tax avoidance and not deterring those keen to take advantage of VCTs and EISs. We consider that the objective of tackling abuse would best be achieved by invoking the GAAR provisions. In that way, it would be unnecessary to further complicate the VCT and EIS legislation.

We welcome the publication by the Government of a paper on the UK priorities for the G20-OECD project for countering Base Erosion and Profit Shifting (BEPS). It is very helpful that the Government has made a significant contribution to the debate around BEPS issues through publishing its views on the matters identified by the OECD. We anticipate that the BEPS process will eventually lead to changes in UK tax law, and the earlier the debate around the changes needed is begun, the greater the chance of effective and proportionate change being the result.

Practicality

We are concerned that the proposals to go ahead with changes to the taxation of Limited Liability Partnerships (LLPs) will take effect from 6 April 2014. The House Of Lords Economic Affairs Committee's Finance Bill Sub-Committee (FBSC) recommended that the changes should be deferred until 2015 to give LLPs time to adapt. While it is right to review the taxation of LLP members to ensure fairness in the tax system, it is disappointing that the FBSC's recommendations have been ignored. The proposed changes are not the same as that originally consulted on last year and were further revised on 7th March. As a matter of fairness and practicality, LLPs need time to consider the legislation, in its final form, to determine whether the legislation applies to them, seek advice where there is doubt and, where applicable, to make appropriate changes.

The new Tax-Free Childcare scores well under this heading. The use of online accounts, with assistance provided for those who can't get online, and the fact that there will be only one provider, National Savings and Investments, should make it easier for families to access, and to benefit from, the new relief. The decision to fix entitlement to Tax-Free Childcare for three-monthly periods, rather than allow it to fluctuate with changes in circumstances as in tax credits, is important. This will avoid the difficulties caused to claimants by constantly changing entitlement, with resulting overpayments and underpayments, and the system will work better as a result.

We welcome the changes around the savings rate also. It has been announced that from 6 April 2015 the starting rate of tax for savings income (such as bank or building society interest) will be reduced from 10% to 0%, and that the maximum amount of taxable savings income that can be eligible for this starting rate will be increased from £2,880 to £5,000. We believe that this is great news for prudent savers on modest incomes.

To address the criticism that the starting rate on savings is administratively so complex that few people claim it, savers who do not expect to be liable to tax on any of their savings income in the tax year will be able to complete a R85 form – the form used to register with a bank or building society for interest to be paid gross (ie without 20% tax deducted at source). Currently an R85 can only be completed by a saver whose total taxable income for the tax year is below their tax-free personal allowance. Without this change, the taxpayer would have to reclaim the tax automatically deducted from their bank interest. This is a welcome change which will enable more taxpayers to benefit from the starting rate on savings.

However, we would caution that people will only complete R85 if they know about it and understand that they are eligible. As LITRG noted in a report published last year, this is often not the case. The onus is now on banks and building societies and HMRC to ensure that the R85 system is better publicised – now more than ever if the changes announced in the Budget are going to have the desired impact on savers' pockets.

We note that the process for an individual to transfer part of their tax allowance to their spouse or civil partner is most likely to be done by an on-line system. HMRC will need to ensure that assistance is available to people who do not have computer access (the digitally excluded) if the proposal is to be practical and fair.

Coherence

The measures on pensions and savings score well under this heading. Rather than tinker around the edges, making small changes that are as likely to complicate matters as they are to benefit taxpayers, the Government has announced a cohesive package of measures which promise wholesale reform of the rules and which give pensioners and savers the flexibility to manage their money. With regard to the changes to savings, we would urge the Government to keep in mind the critical importance of simplicity and not over-complicate the new rules. On pensions, we would emphasise the need for people to obtain good quality advice on what, for many of them, will be the biggest financial decision of their life.

Similar points apply with regard to childcare where the Government intends to replace the current scheme of relief (Employer-Supported Childcare) with the new Tax-Free Childcare. This is a major new scheme of relief, open to significantly more families than previously, and it is important that it is simple to operate and flexible to the changing demands of childcare. We welcome the Government's proposals for the new relief, which we find to be considered and detailed. The Government is to be commended on its willingness to engage with stakeholders on the design of the relief.

Conclusion

As in previous years, we have mixed views on how well this Budget and Finance Bill scores under the Committee's headings. Most of the categories have measures that score well and others that don't. As noted above, we have significant concerns over the Government's proposals to collect disputed tax in advance from users of DOTAS. We believe these measures to be retrospective and that they will weaken DOTAS, damaging confidence in the fairness of the UK tax regime as a result. We regret also that the Government has chosen to make another temporary increase in the amount of the AIA rather than setting this at a sensible level for the conceivable future. With these concerns in mind, we feel that a rating of 7/10 is appropriate.

The Chartered Institute of Taxation

The Chartered Institute of Taxation (CIOT) is the leading professional body in the United Kingdom concerned solely with taxation. The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. The CIOT's work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.

The CIOT draws on our members' experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries. The CIOT's comments and recommendations on tax issues are made in line with our charitable objectives: we are politically neutral in our work.

The CIOT's 17,000 members have the practising title of 'Chartered Tax Adviser' and the designatory letters 'CTA', to represent the leading tax qualification.

The Association of Taxation Technicians

The Association is a charity and the leading professional body for those providing UK tax compliance services. Our primary charitable objective is to promote education and the study of tax administration and practice. One of our key aims is to provide an appropriate qualification for individuals who undertake tax compliance work. Drawing on our members' practical experience and knowledge, we contribute to consultations on the

development of the UK tax system and seek to ensure that, for the general public, it is workable and as fair as possible.

Our members are qualified by examination and practical experience. They commit to the highest standards of professional conduct and ensure that their tax knowledge is constantly kept up to date. Members may be found in private practice, commerce and industry, government and academia.

The Association has over 7,500 members and Fellows together with over 5,000 students. Members and Fellows use the practising title of 'Taxation Technician' or 'Taxation Technician (Fellow)' and the designatory letters 'ATT' and 'ATT (Fellow)' respectively.

The Low Incomes Tax Reform Group

The Low Incomes Tax Reform Group (LITRG) is an initiative of the Chartered Institute of Taxation (CIOT) to give a voice to the unrepresented. Since 1998 LITRG has been working to improve the policy and processes of the tax, tax credits and associated welfare systems for the benefit of those on low incomes. Everything we do is aimed at improving the tax and benefits experience of low-income workers, pensioners, migrants, students, disabled people and carers.

LITRG works extensively with HM Revenue & Customs and other government departments, commenting on proposals and putting forward our own ideas for improving the system. Too often the tax and related welfare laws and administrative systems are not designed with the low-income user in mind and this often makes life difficult for those we try to help.

The CIOT is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT's primary purpose is to promote education and study of the administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.

Appendix 2: Institute of Chartered Accountants in England and Wales

Traffic light assessment

The Treasury committee has six principles for tax policy: that it should be **fair, support growth and competitiveness, certain** (i.e. legally clear, targeted and simple), **stable, practical, and coherent**. We have assessed how Budget 2014's new tax policies match up to the principles.

Measure	Fair?	Supports growth?	Certain?	Stable	Practical	Coherent	OVERALL
Pensions reform	●	●	●	●	●	●	●
Personal allowance Increase in allowance by £500 to £10,500	●	●	●	●	●	●	●
Annual investment Allowance doubled Increase in tax relief for business investment	●	●	●	●	●	●	●
Anti-avoidance: £4bn revenue Increased funding for HMRC non-compliance team	●	●	●	●	●	●	●
HMRC power to access debtor accounts	●	●	●	●	●	●	●
15p stamp duty land tax and ATED on £500,000 properties in corporate entities	●	●	●	●	●	●	●
Seed Enterprise Investment Scheme made permanent	●	●	●	●	●	●	●
Increased limits for ISAs and abolition of distinctions between cash and share based savings	●	●	●	●	●	●	●
Starting rate of tax for savings income	●	●	●	●	●	●	●
5% cut in Bingo Duty	●	●	●	●	●	●	●

Key

-  Pass
-  Neutral
-  Fail

About ICAEW

ICAEW is a professional membership organisation, supporting 140,000 Chartered Accountants who advise over 1.5 million UK businesses. Under our Royal Charter, our world-leading Tax Faculty works closely with HMRC up to a year ahead of every Budget to help strengthen and inform new tax law, in the public interest.

Detailed comments***Pensions reform***

Abolishes rules mandating DC pension holders to buy an annuity or use income drawdown, or face a 55% tax charge on unauthorised withdrawals.

- This transformational reform will free individuals to take what they want, when they want, from their pension savings.
- Good, impartial advice will be critical. We are concerned that the £20 million offered in the Budget is unlikely to be sufficient to fund this. An estimated 400,000 annuities are taken out each year, so this is just £50 per annuitant.
- Withdrawals will be taxed at marginal rates, boosting tax receipts by £5bn over five years.
- Taxpayers will still be able to access a tax-free lump sum.
- The government needs to clarify what will happen to those who exhaust their pension fund too soon, and later become a burden on the state.

Personal allowance increased by £500 to £10,500

- Combined with the removal of the 10% tax rate for the first £5,000 savings income, this will remove many people from income tax and will be welcomed particularly by pensioners.

Annual investment allowance (AIA) doubled to £500,000, until end of 2015

- The annual investment allowance (AIA) is increased from £250,000 to £500,000 for expenditure incurred between 1 April 2014 and 31 December 2015 – so availability is extended and the amount is doubled. The relief is given for capital expenditure on plant and machinery, and to integral features in buildings.
- This will be welcome news for businesses looking to invest, although the continued changes to the limits, and confusing transitional rules each time the limits are

changed, make it more difficult for businesses to plan. Businesses tell us that certainty is the most important factor for them. ICAEW expects business investment to increase this year to 7.1%.

Anti-avoidance: £4bn revenue forecast, increased funding for HMRC non-compliance team

- The Chancellor has recognised that funding HMRC's compliance activities (in effect its credit-control department) is money well spent. However, predicting increased revenues from tax compliance activity is notoriously difficult. The amounts actually collected have often been lower than forecast – for example the actual receipts from the Swiss tax agreement.
- If past experience is a guide, these estimates may well prove to be optimistic. We would wish to probe in detail how these figures have been calculated.

HMRC power to access debtor accounts

HMRC will have the power to take money directly from the bank accounts of tax debtors who owe more than £1,000 in tax or tax credits.

- This proposal is of considerable concern to many taxpayers and accountants. This power is unprecedented in the UK. Other than a comment that a minimum of £5,000 would be left in debtors' accounts, the announcement contains no details of any judicial or other safeguards that could protect taxpayers. It is likely to be particularly serious for those on low incomes struggling with debt problems.
- HMRC has said it will only use this new power where debtors 'have the financial means to pay' and have been contacted multiple times. How will this be determined, and how up-to-date are HMRC's databases? We have seen numerous cases recently of HMRC chasing debts which are not due, including attempting to confiscate assets.
- These powers are extremely worrying, and excessive. Adequate safeguards are essential. What steps will be put in place to ensure funds that are not due are not seized and/or hardship does not follow seizure of funds?
- We note that Crown preference was abolished long ago in bankruptcy proceedings, yet HMRC is effectively to become a preferential creditor under these new rules. We are concerned about this in principle and it could lead to perverse effects – for example holding money in cash rather than in a bank account?

15% stamp duty land tax on £500,000 residential properties in corporate entities

The new higher rate of SDLT will apply to purchases by 'certain non-natural persons' of residential properties with effect from 20 March 2014. The related annual tax on enveloped dwellings (ATED) will also apply to these properties and is being introduced progressively between 1 April 2015 and 1 April 2016.

- We are concerned that by lowering the threshold from £2 million to £500,000, will bring many more properties will now be caught by the measure, bringing many more taxpayers within an onerous compliance regime . Those purchasing £2 million properties are likely to be suitably well advised but this may not be the case further down the scale, leading to the possibility of widespread non-compliance.
- Lowering the threshold will bring many more non-natural persons (NNPs) into the regime but a large number will qualify for relief, for example because they are let on a commercial basis. But they will still need to file a return to claim the relief. The announcement does recognise that the administration of ATED will need to be simplified. There will be a consultation on how this could be achieved.
- For those NNPs who will not qualify for relief, the delayed and staged introduction of the ATED charge to lower value properties will allow time to consider exit plans.

Seed Enterprise Investment Scheme made permanent

- We welcome the announcement that the Seed Enterprise Investment Scheme (SEIS) has been made permanent. This will assist start-ups looking to finance their growth ambitions.
- We remain concerned at the complexity of the scheme, which causes many investors unexpectedly to fail to qualify.

Increased limits for ISAs, abolition of distinctions between cash and share-based savings

- Proposals to increase the limits for ISAs and abolish distinctions between cash and share-based savings will be welcomed by many, as will the announcement of new bonds with higher interest rates.
- Savers have been particularly hard hit by a long period of low interest rates and poor annuity returns, so these changes will be well received by pensioners and savers.

Abolishing 10% starting rate for savings income

Anyone with total income under £15,500 pa will not pay any tax on savings income. From 6 April 2015 the starting rate of tax for savings income (such as bank or building society interest) will be reduced from 10% to 0% and the maximum amount of taxable savings income that can be eligible for this starting rate will be increased from £2,880 to £5,000. Taken together with the new personal allowance for 2015/16 of £10,500, this means that most savers won't be liable for tax until their total taxable income exceeds £15,500.

- Savings income is usually taxed at source, with the bank or building society deducting income tax at the basic rate of 20%. If the account holder is a non-taxpayer, they either have to reclaim the tax overpaid, or take action so that they receive their interest gross, by registering with their bank or building society. The success of this measure will rely heavily on banks promoting the gross payment

option. People who have savings income which is only partly taxable cannot be paid gross but will have to reclaim any overpaid tax through the tax system and will need to be made aware of the process.

- It will be vital that a taxpayer keeps track of the level of their income as the year progresses, because if their income exceeds the level at which no tax is payable, they must tell their bank.

Appendix 3: Association of Certified Chartered Accountants

About ACCA

ACCA is the global body for professional accountants. We aim to offer business-relevant, first-choice qualifications to people around the world who seek a rewarding career in accountancy, finance and management.

ACCA has 162,000 members and 428,000 students in 173 countries, with 64,000 members and 79,000 students in the UK, and works to help them to develop successful careers in accounting and business, with the skills required by employers. We work through a network of over 89 offices and centres and more than 8,500 Approved Employers worldwide, who provide high standards of employee learning and development. Through our public interest remit, we promote appropriate regulation of accounting and conduct relevant research to ensure accountancy continues to grow in reputation and influence.

The expertise of our senior members and in-house technical experts allows ACCA to provide informed opinion on a range of financial, regulatory, public sector and business areas, including: taxation (business and personal); small business; pensions; education; and corporate governance and corporate social responsibility.

Comments on the Budget

1. In March 2011, the Treasury Committee set out six principles by which it recommended tax policy should be measured. This memorandum seeks to comment at a high level on the extent to which the measures announced in the Budget comply with those principles.

2. The Principles are in summary that tax policy should:

- be fair;
- support growth and encourage competition;
- provide certainty;
- provide stability;
- Tax policy should be practicable; and
- Finally, the tax system as a whole must be coherent.

3. As the global body for professional accountants, ACCA welcomes the elements of this budget which embrace global principles for better taxation which support enterprise. The budget includes a number of measures specifically targeted to enhance investment, encourage compliance and foster a responsible attitude to spending. ACCA in particular welcomes the paper *“Tackling aggressive tax planning in the global economy: UK priorities for the G20-OECD project for countering base erosion and profit shifting”*.

4. As has been widely acknowledged, the issues facing domestic tax authorities in addressing the perceived structural weaknesses in the interaction between sovereign tax jurisdictions and global cross border business forms require coordinated, coherent and consistent action from as many actors as possible. ACCA fully supports, and is committed to facilitating and contributing to, this process.

5. ACCA welcomes also the OTS paper published alongside the budget, "*Competitiveness review: initial thoughts and call for evidence*". The paper considers the relative performance of the UK in global terms, but also makes the very valid point that comparative performance is not the only driver. Simplification and improvement of the UK system is a valid and indeed a compelling driver in its own right.

6. This Budget has seen less in the way of undue complexity than has perhaps been the case in previous budgets, and to the extent that there provisions likely to cause significant practical difficulties for taxpayers, advisers or HMRC they are confined to the anti-avoidance arena.

7. However, the pace and nature of developments in the anti-avoidance field have given some cause for concern. The Government has continued to share a significant proportion of the draft clauses for the Finance Bill in December, and this is welcome. While the scope for detailed scrutiny is to some extent restricted by the Christmas break, there is an inevitable compromise between the interests of officials and Ministers preparing the policies and legislation and the interests of those stakeholders engaged in the consultation and review process.

8. It is notable that the clauses exposed for consultation in December included elements of anti-avoidance legislation, such as the onshore intermediaries rules and the revisions to partnership taxation. It is of course not always possible to consult widely on anti-avoidance legislation and any opportunity for compliant businesses which may be caught up in the impact of such provisions is welcome.

9. Even so, there have been a number of calls in respect of both these provisions and other aspects of the anti-avoidance legislation to allow more time for consultation and consideration of the legislation, and for compliant businesses and advisers to adapt to the proposals. The changes to the taxation of partnerships will impose on many genuine existing businesses a need to fundamentally revise their terms and manner of operation. Although there had been some prior consultation over the summer of 2013, the draft clauses which were published in December were a departure from the existing direction of discussions and have caused significant widespread concern among businesses and their advisers. However, while some minor changes were announced at the end of the consultation period on the draft clauses, the implementation of the measures is to press ahead.

10. In the complex area of employment status for tax purposes, the government consulted widely with interested bodies and has responded with a number of changes to the proposals for onshore intermediaries, and some revisions to the timing of their implementation. Nevertheless, there are still some fundamental areas of concern, particularly around the practicalities of the interaction with compliant PSCs. The process for managing information flow along the contractual chain is also an area of concern, with

worries that the industry will struggle to set up ICO compliant processes which will satisfy both the commercial concerns of taxpayers and the information requirements of HMRC.

11. While the timing is an issue, another theme runs through the intermediaries and partnership measures. Both involve the government's reaction to taxpayer responses to tax measures which are themselves a function of the landscape of business form and corporate laws in the UK. Tax, as a matter of simple practicality, is aligned to legal form. Resolution of the underlying tensions between economic substance and legal form where the two might diverge is key to the efficiency of the system.

12. At the same time, the tax system is often used as a mechanism to encourage or reward certain legal forms. For example, while employees make a greater proportional contribution to the exchequer from their earnings than the self employed, they receive a greater return in social security protections. Conversely, the rate of tax on invested capital is (currently) lower, and measures such as the SEIS encourage further investment in equity.

13. The final proposals to revise the treatment of partnerships and provision of services and labour represent adjustments to aspects of the system which are fundamental to decisions about business form and commercial operation. They deserve more than 4, 8 or 12 weeks of consultation. The changes in each case are recognised by HMRC to potentially have significant impacts upon compliant taxpayers. The Finance Bill Sub-Committee of the House of Lords Economic Affairs Select Committee urged a delay in implementation of the partnership provisions to give time for business to react to the changed economic landscape, and ACCA supports that call for a measured approach to such fundamental reform.

14. The field of marketed tax avoidance schemes has also been the focus of considerable government attention, with consultations starting over the summer of 2013. Again however, the scope of proposals has grown and changed over the course of the consultation process. There is universal agreement among the professional bodies that artificial and contrived schemes whose sole purpose is generation of a tax advantage through abuse of the rules is a legitimate target for focused and proportionate measures. However, the breadth and scope of the powers outlined in respect of high risk tax agents prompted expressions of concern from many that there were significant potential risks to compliant tax payers.

15. In December 2013, indications of a further extension of HMRC powers to tackle users of such schemes through the 'follower notice' mechanism were given, and again prompted expressions of concern from advisers. In late January 2014, at the height of the personal tax filing season for individuals and the yearend reporting process for big business, the detail of the follower notice regime and the related accelerated payment provisions were published. The consultation period was just four weeks. Despite the brevity of the consultation period, and the business pressures upon them, the proposals provoked an unprecedented response from ACCA members, unanimously opposing the radical extension of HMRC powers.

16. The budget itself saw the announcement of an HMRC power to take money directly from taxpayers' bank accounts. While we understand that there will be a number of safeguards around the measure to prevent abuse, or the infliction of consequential

hardship on those relying upon the relevant accounts either directly or indirectly, it is vital that HMRC manages taxpayer expectations and operates any such power in a transparent and proportional manner. While it might be characterised as simply the equivalent of distraint powers, and exercised in similar circumstances, the fact remains that the potential side effects could be catastrophic for wrongly targeted taxpayers. As is noted elsewhere, HMRC is dependent upon the goodwill of taxpayers, and misuse of such powers would rapidly erode trust and goodwill.

17. Again, the speed of change raises concerns. In particular, the indications that much of the material has been developing internally for months if not years without any external consultation are a concern. The particular confluence of circumstances which contribute to the apparently compelling arguments for introducing these new powers are the result of temporary circumstances in a fast moving area. Introduction of permanent powers which would previously have been rejected by many commentators out of hand should be approached with caution and safeguards, and ideally in time limited form.

18. The Budget includes a number of measures designed to enhance investment, research and development. However it is notable that the measures in this budget, and previous budgets, can be characterised as displaying a piecemeal approach to incentives. Welcome as the incentives are, a more structured long term approach to them would increase the confidence of business in the long term stability of the tax system.

19. The continued extension to the scope of the Annual Investment Allowance is an example of a measure designed to encourage investment and growth but whose effect may be diluted by complexity of application. As has been noted previously, implementation of the enhanced limit from 1 January requires businesses who do not have a 31 December year end to apportion their income. This is the fifth different rate of allowance in 7 years, hardly the stability called for by the Committee. The stimulus is welcome; the additional complexity, the burden of which will be disproportionately felt by SME businesses, is not.

20. There is of course a further aspect to the availability of the enhanced annual investment allowance, and that is that many businesses may have suffered uninsured losses as a result of flooding and other extreme weather conditions in recent months. While no more than a silver lining at best, the ability to replace plant up to £500,000 with immediate tax relief and no further administrative burdens will be welcome.

21. The last of the Committee's principles is that the tax system as a whole should be coherent. The introduction of the Corporate Tax Roadmap has been widely recognised as a positive step towards coherence of the system for taxation of incorporated businesses in the UK. However, the majority of active businesses by number in the UK are not incorporated, and in many cases the taxation of their profits is effectively assessed under personal tax rules.

22. Taxation for most individuals is a 'fact of life', and the interaction of the tax system with household budgeting is limited to the impact of changes in tax rates. The development of long term policy is of limited relevance, as in most cases individuals are unable to arrange their affairs so as to take any particular advantage of knowing what the structure of liabilities may be in two or three years' time.

23. For businesses on the other hand, prediction of after tax returns is a significant ingredient in long term commercial success, while modelling of cashflows is fundamental to short term survival, especially for smaller businesses which may not have reserves. What is needed is not so much a personal tax roadmap as a business tax roadmap – and ideally one which incorporates NICs as well. Changes in the approach to employers' NICs impact directly upon business profits, and while the setting of rates is beyond the scope of the Committee's work, and will always inevitably remain a short term political decision, any guidance for business would improve the ability to plan ahead.

24. In any event, the impact on a single business of rate changes in personal tax is likely to be lower than that of corporate tax. A 1% rise in income tax rates would deliver a similar amount to a 4% rise in corporation tax rates based purely on rates, but the impact of behavioural change would likely increase the disparity, as companies are more able and willing to plan to mitigate their exposure to tax rises.

25. The vast majority of tax receipts come in with no active intervention or management from HMRC, whether through PAYE or self-assessment for income or corporate tax. Even so, current projections indicate that by the end of this parliament the yield from HMRC interventions will have doubled. There is an increasing focus on potentially high yield taxpayers, and it is notable that in both the personal and corporate tax arena a significant proportion of all receipts comes from a comparatively small number of high value taxpayers.

26. It is vital that the voluntary compliance of the majority of taxpayers is not taken for granted. There is anecdotal evidence from practitioners that some small businesses are developing an attitude that if 'big business' is going to seek to avoid tax then they too will look for any opportunity to reduce the amounts paid to HMRC. Unfortunately it is of course the case that for many small businesses the lack of complexity in their tax affairs means that the only scope to influence the ultimate tax liability is to somehow suppress the reported profit. The erosion of taxpayer goodwill is a significant possible threat to wider revenues and must be resisted.

27. Overall, the 2014 Budget has delivered a coherent package of measures which for the most part continue the direction of travel towards the principles of good taxation. In order to maintain that movement, ACCA would welcome the extension of the corporate tax road map to business tax more generally, and the adoption of a more measured approach to fundamental changes to the environment for businesses.

Formal Minutes

Wednesday 7 May 2014

Members present:

Mr Andrew Tyrie, in the Chair

Mark Garnier	Jesse Norman
Mr Andrew Love	Teresa Pearce
John Mann	David Ruffley
Mr Pat McFadden	John Thurso
Mr Brooks Newmark	

Draft Report (*Budget 2014*), proposed by the Chair, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 270 read and agreed to.

Papers were appended to the Report as Appendix 1, Appendix 2 and Appendix 3.

Resolved, That the Report be the Thirteenth Report of the Committee to the House.

Ordered, That the Chair make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

Written evidence was ordered to be reported to the House for publication on the internet.

[Adjourned till Tuesday 10 June at 9.45am]

Witnesses

Tuesday 25 March 2014

Paul Mortimer-Lee, Global Head, Market Economics, BNP Paribas, **Michael Saunders**, Head of West European Economics, Citi, and **Robert Wood**, Chief UK Economist, Berenberg Bank

[Q1-51](#)

Paul Johnson, Director, Institute for Fiscal Studies, and Gemma Tetlow, Programme Director, Pensions, Savings and Public Finance, Institute for Fiscal Studies

[Q52-97](#)

Wednesday 26 March 2014

Robert Chote, Chairman, Office for Budget Responsibility, **Steve Nickell CBE**, Member, Budget Responsibility Committee, and **Graham Parker CBE**, Member, Budget Responsibility Committee

[Q98-211](#)

Tuesday 1 April 2014

Chris Woolard, Director of Policy, Risk and Research, Financial Conduct Authority, and **David Geale**, Head of Savings, Investments and Distribution, Financial Conduct Authority

[Q212-268](#)

Dr Ros Altmann, Pensions Policy, Investment Banking, Savings and Retirement Expert, and **Jane Vass**, Head of Public Policy, Age UK

[Q269-294](#)

Chris Hannant, Director General, Association of Professional Financial Advisors, **Robin Fieth**, Chief Executive, Building Societies Association, and **Joanne Segars**, Chief Executive, National Association of Pension Funds

[Q295-358](#)

Thursday 3 April 2014

Rt Hon George Osborne MP, Chancellor of the Exchequer, **Sir Nicholas Macpherson KCB**, Permanent Secretary, HM Treasury, and **James Bowler**, Director, Strategy, Planning and Budget, HM Treasury

[Q359-442](#)

Tuesday 8 April 2014

Otto Thoresen, Director General, Association of British Insurers

[Q443-494](#)

Frank Haskew, Head of Tax Faculty, Institute of Chartered Accountants in England and Wales, **Patrick Stevens**, Tax Policy Director, Chartered Institute of Taxation, and **Andrew Courts**, Member, ACCA Global Tax Forum

[Q495-547](#)

List of additional written evidence

(Available on the Committee's website:

<http://www.parliament.uk/business/committees/committees-a-z/commons-select/treasury-committee/inquiries1/parliament-2010/budget-2014/?type=Written#pnIPublicationFilter>)

- 1 [Chartered Institute of Taxation \(B140001\)](#)
- 2 [BNP Paribas \(B140003\)](#)
- 3 [Association of Chartered Certified Accountants \(B140004\)](#)
- 4 [Institute of Chartered Accountants in England and Wales \(B140005\)](#)
- 5 [Letter from Otto Thoresen, Director General, ABI to John Griffith-Jones \(B140006\)](#)
- 6 [Letter from Tidjane Thiam, Chairman, ABI to Rt Hon George Osborne MP \(B140007\)](#)
- 7 [AGE UK—Supplementary written evidence \(B140008\)](#)
- 8 [Letter from David Gauke MP, Exchequer Secretary to the Treasury \(B140009\)](#)
- 9 [CBI \(B140010\)](#)
- 10 [Institute of Chartered Accountants in England and Wales—Supplementary written evidence \(B140011\)](#)
- 11 [Building Societies Association—Supplementary written evidence \(B140012\)](#)

List of Reports from the Committee during the current Parliament

Session 2010–12

First Report	June 2010 Budget	HC 350
Second Report	Appointment of Dr Martin Weale to the Monetary Policy Committee of the Bank of England	HC 475
Third Report	Appointment of Robert Chote as Chair of the Office for Budget Responsibility	HC 476
Fourth Report	Office for Budget Responsibility	HC 385
Fifth Report	Appointments to the Budget Responsibility Committee	HC 545
Sixth Report	Spending Review 2010	HC 544
Seventh Report	Financial Regulation: a preliminary consideration of the Government's proposals	HC 430
Eighth Report	Principles of tax policy	HC 753
Ninth Report	Competition and Choice in Retail Banking	HC 612
Tenth Report	Budget 2011	HC 897
Eleventh Report	Finance (No.3) Bill	HC 497
Twelfth Report	Appointment of Dr Ben Broadbent to the Monetary Policy Committee of the Bank of England	HC 1051
Thirteenth Report	Appointment of Dr Donald Kohn to the interim Financial Policy Committee	HC 1052
Fourteenth Report	Appointments of Michael Cohrs and Alastair Clark to the interim Financial Policy Committee	HC 1125
Fifteenth Report	Retail Distribution Review	HC 857
Sixteenth Report	Administration and effectiveness of HM Revenue and Customs	HC 731
Seventeenth Report	Private Finance Initiative	HC 1146
Eighteenth Report	The future of cheques	HC 1147
Nineteenth Report	Independent Commission on Banking	HC 1069
Twentieth Report	Retail Distribution Review: Government and FSA Responses	HC 1533
Twenty-first Report	Accountability of the Bank of England	HC 874
Twenty-second Report	Appointment of Robert Jenkins to the interim Financial Policy Committee	HC 1575
Twenty-third Report	The future of cheques: Government and Payments Council Responses	HC 1645
Twenty-fourth Report	Appointments to the Office of Tax Simplification	HC 1637
Twenty-fifth Report	Private Finance Initiative: Government, OBR and NAO Responses	HC 1725
Twenty-sixth Report	Financial Conduct Authority	HC 1574
Twenty-seventh Report	Accountability of the Bank of England: Response from the Court of the Bank	HC 1769
Twenty-eighth Report	Financial Conduct Authority: Report on the Governments Response	HC 1857
Twenty-ninth Report	Closing the tax gap: HMRC's record at ensuring tax compliance	HC 1371
Thirtieth Report	Budget 2012	HC 1910

Session 2012–13

First Report	Financial Services Bill	HC 161
Second Report	Fixing LIBOR: some preliminary findings	HC 481
Third Report	Access to cash machines for basic bank account holders	HC 544
Fourth Report	Appointment of Mr Ian McCafferty to the Monetary Policy Committee	HC 590
Fifth Report	The FSA's report into the failure of RBS	HC 640
Sixth Report	Appointment of John Griffith-Jones as Chair-designate of the Financial Conduct Authority	HC 721
Seventh Report	Autumn Statement 2012	HC 818
Eighth Report	Appointment of Dr Mark Carney as Governor of the Bank of England	HC 944
Ninth Report	Budget 2013	HC 1063

Session 2013–14

First Report	Appointments of Dame Clara Furse, Richard Sharp, and Martin Taylor to the Financial Policy Committee	HC 224
Second Report	Appointments of Dr Donald Kohn and Andrew Haldane to the Financial Policy Committee	HC 259
Third Report	Spending Round 2013	HC 575
Fourth Report	Re-appointment of Professor Stephen Nickell to the Budget Responsibility Committee	HC 688
Fifth Report	Appointment of Sir Jon Cunliffe as Deputy Governor of the Bank of England	HC 689
Sixth Report	Re-appointment of Dr Martin Weale to the Monetary Policy Committee	HC 313
Seventh Report	Money Advice Service	HC 457
Eighth Report	OBR Fiscal Sustainability Report 2013	HC 958
Ninth Report	Autumn Statement 2013	HC 826
Eleventh Report	Appointment of Spencer Dale to the Financial Policy Committee	HC 1236
Twelfth Report	Appointment of Andy Haldane to the Monetary Policy Committee	HC 1235
Thirteenth Report	Budget 2014	HC 1189
