Inquiry of the Work and Pensions Select Committee on pension freedom guidance and advice
Response from the Low Incomes Tax Reform Group (LITRG)

1 Executive Summary and recommendations

1.1 We welcome the opportunity to give evidence to the inquiry into the guidance and advice on offer to people navigating the "choice and flexibility" which has arisen as a result of the changes to pensions introduced in April 2015.

1.2 Our response concentrates on those areas which are of relevance to both the taxation of those on low incomes and their entitlement to state benefits.

1.3 People need to be well informed about both the income tax and state benefit consequences of the choices they make with their pension funds. These choices will affect their income for the remainder of their lives, with no opportunity to correct inadvertent mistakes.

1.4 Failure to deliver clear and correct guidance is likely to create additional burdens on HMRC in the form of contact from ill-informed taxpayers. For the taxpayers themselves, likely consequences include failure to understand how their retirement income will be taxed, what their obligations to report this income are and (possibly) a reduction in their entitlement to state benefits.

1.5 The Committee will appreciate that many individuals face a significant reduction in their income when they retire. We believe that Pension Wise must:

- review the guidance it offers to ensure it is tailored to each individual's circumstances to ensure that people make the right decision;

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- review the accessibility of the provision of face-to-face meetings particularly for individuals in remote locations;
- expand the network of organisations which signpost individuals to its services; and
- improve the online links to its websites from other organisations

1.6 HMRC must ensure that their staff are fully aware of the tax issues surrounding the new flexibility and should consider establishing a specialist team to deal with people's enquiries and take the necessary action promptly.

2 About Us

2.1 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.

2.2 LITRG works extensively with HM Revenue &Customs (HMRC) 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.

2.3 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.

3 Tax guidance and advice

3.1 LITRG responded in detail to the FCA's Consultation Paper 14/11.[1] We are disappointed that, based on the requirements placed upon both guidance providers and paid for advisers outlined in Appendix 1, many of our concerns have been overlooked. We therefore welcome the opportunity to reiterate these here.

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[1] LITRG's response can be found at http://www.litrg.org.uk/Resources/LITRG/Documents/2014/09/140922_LITRG%20response%20FCA%20Retirement%20Guidance%20Guarantee%20FINAL.pdf

3.2 ***The tax charities' experience***

3.2.1 We are also able to provide details of the types of enquiries that the two Tax charities, Tax Help for Older People and TaxAid[1] have received.

3.2.2 TaxAid has received 15 enquiries relating to the new pensions freedoms, mainly from low-income clients of working age. Tax Help for Older People, which mainly advises low-income pensioners and those approaching pension age, has received 293 such enquiries.

3.2.3 Of those consulting TaxAid:

- four had not heard of the Pension Wise service and so were signposted to it by the TaxAid adviser;
- three (including one of the individuals signposted to Pension Wise who subsequently came back to TaxAid) wanted specific tax calculations so that they could include the after-tax amount in their decision-making process;
- one had been signposted to TaxAid by Pension Wise to provide tax advice;
- two had questions surrounding their entitlement to state benefits as well as needing details of the after-tax amount which they might receive;
- two had claimed tax refunds but been refused by HMRC because they were in receipt of ESA;
- one wished to claim a refund but had not been able to contact HMRC;
- two appeared to be not resident in the UK and needed general as well as tax specific advice. In both instances they were signposted towards professional advice;
- one was signposted to professional legal advice as his enquiry concerned the post divorce allocation of his pension pot.

3.2.4 Our initial concern is that some of the individuals who called TaxAid were not aware of the Pension Wise service. All the individuals had managed to find the contact details for TaxAid, a small charity with limited means of publicising its services, but had failed to do so for Pension Wise. We recommend that Pension Wise should consider how it might:

- expand the network of organisations which signpost individuals to its services; and
- improve the online links to its website from other organisations.

3.2.5 Helping individuals who are tax resident outside the UK is difficult as their position will be determined by both the UK tax and pension environment and that of the overseas country in

[1] Tax Help for Older People is a service provided by Tax Volunteers, registered charity no. 1102276, which gives pro bono professional help for older people who cannot afford to pay for such tax advice. TaxAid, registered charity no. 1062852, provides pro bono professional help for people of all ages who cannot afford to pay for such tax advice.

which they are resident. The UK has double tax treaties with many countries which may ensure that pension income and/or lump sum(s) are only taxed once but the new legislation may bring problems that could not occur under the old system, for example, are regular but infrequent withdrawals classified as income or capital?

3.2.6 Individuals with such complications need to be signposted to qualified advisers. The Pension Wise website has a section relating to living abroad[1] but we would recommend that it refines its website search mechanism. We searched on “not UK resident” and “I live abroad” and were taken to the section but when we used the search terms “I live in France” and “I live outside the UK” we were not.

3.2.7 HMRC will need to ensure that any necessary forms, for example form R43, are updated to enable in-year tax refund claims to be made when non UK residents access their UK pension pots. We are concerned that low-income taxpayers living abroad will be unable to afford professional advice or will find it difficult to access and we would urge that HMRC adopt a sympathetic approach to such individuals.

3.2.8 The number of enquiries Tax Help for Older People has received about the new pensions freedom makes it difficult to categorise by subject matter. One example however indicates individuals’ expectations and how this is affected by the PAYE system.

3.2.9 An individual was in need of money to pay off a debt. As he had no other income he withdrew £10,600 (the 2015/16 tax free personal allowance). However, in accordance with PAYE regulations, this amount was taxed under PAYE by the pension company. The individual completed HMRC’s form P55 to reclaim the tax. This form is for individuals who have

- taken some money from their pension pot; and
- do not intend to take any further payments from their pension pot in the tax year.

3.2.10 Completion and submission of the P55 should generate an appropriate refund of the PAYE withheld by HMRC within 30 days.

3.2.11 HMRC, incorrectly, told the individual that this could not happen and that, in order to generate the refund through the PAYE system, they would send a PAYE code to the pension company and that the individual would have to make a second withdrawal which would generate the refund through the PAYE system. The individual duly did so. However, the pension company had not received the PAYE code and once again taxed the second withdrawal.

3.2.12 This example demonstrates our belief that the tax implications of retirement income options must include clear information. A great many individuals will simply not understand their pensions and how they are taxed, or if they are taxable at all. Indeed, pensioners often do not know that the state pension is taxable, let alone the complex fashion in which it is

[1] https://www.pensionwise.gov.uk/living-abroad

taxed.[1] The information provided should not just inform the individual as to whether or not the sums received are taxable, but also how and when the tax due will be collected. It is highly unlikely that any tax collected under the PAYE system, particularly in respect of larger lump sums or irregular payments, will be correct. Individuals will firstly need to understand that they may either owe more tax or be due a refund of tax. Then they will have to establish how to pay this tax or claim their refund. Will the individual need to complete a SA tax return? Our concerns are backed up by the fact that all of the individuals (bar one) who contacted TaxAid, and all who contacted Tax Help for Older People, wanted advice on their tax position.

3.3 ***Tax and benefits consequences of flexible withdrawal***

3.3.1 These pension reforms will mean that individuals who are still in work may withdraw significant sums from their pension funds. They will need to understand the effect that this will have the on the after-tax amount that they receive. For example, people with families who withdraw from their pension schemes and increase their income into or through the £50,000 to £60,000 band will experience not only higher rates of tax, but also lose some or all of their child benefit. Individuals might be able to make significant tax savings by, for example, simply splitting a lump sum payment between two tax years. An individual might lose their ability to utilise the transferable marriage allowance. It is low-income taxpayers who will benefit most from guidance and advice with respect to these issues and they are the ones least likely to be able to afford it.

3.3.2 We are also concerned that guidance providers and advisers are unlikely to have sufficient knowledge of the impact of their guidance on the state benefits entitlement of the individual. This concern is supported by the enquiries received by TaxAid outlined above. Even the state pension is not straightforward, with the possibility of deferring a claim to it (and consequent tax impact for the individual, with state pension deferral having its own, peculiar, regime).

3.3.3 As an example, the FCA's policy statement PS15-05 at clause 3.34 asks:

"Is the consumer aware that taking money from their pension may impact on any means-tested benefits they receive?"

3.3.4 However, for pension credit, failure to take money from a pension might impact on an individual's entitlement to pension credit as explained in the DWP factsheet "Pension flexibilities and DWP benefits"[2] published in March 2015.

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[1] The DWP is unable to deduct tax directly from the state pension. Tax due is therefore collected either by adjusting the individual's PAYE code in respect of other pension or employment income or directly from the taxpayer.

[2] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/417473/pension-flexibilities-dwp-benefits.pdf

3.3.5 There may also be issues around the nature of the amount received, i.e. capital or income. In most cases this will be straightforward, e.g. when all the pension fund is taken as a lump sum, but there may be other circumstances which are more open to interpretation. Added to these are the ways in which different benefits calculate an individual's relevant income, for example:

- is the income amount to be included before or after tax?
- is the tax that should be deducted the actual liability or the amount initially deducted at source from the income?

3.3.6 These are all issues which may impact on an individual's position. Our concern is that if a guidance provider or adviser does not recognise there is an issue, then they will fail to signpost the individual to additional advice or provide adequate guidance on the points on which the individual needs to take such advice.

3.4 ***Face-to-face advice***

3.4.1 In our response to FCA's CP 14/11 we highlighted various other issues, two of which are worth reiterating here.

3.4.2 As the Committee will be aware, the FCA's response to the Committee's Report, 2014-15 identified that demand for face-to-face interviews through the Pension Wise service has been significantly less than estimated:

"*Telephone demand has been close to the Government's original estimates, but face-to-face demand has been much lower; only 10-15 per cent of Citizens Advice capacity has been used."*

3.4.3 The Committee will appreciate that this statement does not make it clear whether more individuals would have chosen a face-to-face interview if one had been available within a reasonable distance and/or within a reasonable time scale. The Citizens Advice Bureau's website indicates that Pension Wise appointments are available at 500 locations across England and Wales; again the Committee will appreciate that this provides no indication of the geographical spread or accessibility of these locations.

3.4.4 The lower paid may find it more difficult to take time off work to attend face-to-face meetings if these are only held during normal working hours (one of our colleagues phoned to make an appointment and was offered 12:00 or 13:30). Individuals who are disabled or unwell may find it difficult to travel. The costs of travel and the time involved will also limit the numbers of individuals who will be able to attend face-to-face sessions.

3.4.5 One of our colleagues attended a guidance session at her local CAB office during August. On a positive note she was offered an appointment within four days of her enquiry and at a location that was close to her home and easily accessible. These facts reflect the lack of take-up of the face-to-face sessions and also that our colleague lives in London. By contrast a colleague who lives in the South West would have to travel two hours by car to the nearest CAB offering guidance and the journey by public transport would take longer and involve three bus and one train journey each way. The Pension Wise website also appears to use an "as the crow flies" location finder; a colleague on the Scottish mainland was signposted to locations on the Islands of Skye and Harris which were only closer because they required a journey by boat.

3.4.6 The adviser was approachable and friendly but referred constantly to her guidance notes and was unable to explain coherently the difference between the "adjustable income" option (flexi-access drawdown) and the "taking cash in chunks option" (uncrystallised funds pension lump sum).

3.4.7 We can provide, if required, an anonymised copy of the guidance document which our colleague received. There is little mention in the document of the effect on state benefits of making withdrawals, although our colleague told the adviser that she was not in receipt of state benefits and did not expect to be so in the future.

3.4.8 On a positive note our colleague received this document by post five days after the meeting. However, the guidance provided is wholly generic and could be obtained from other sources. It is not tailored to the information that our colleague provided. As an example our colleague has several different pension pots and so would be able to treat each pot separately; this is not highlighted in any way in the document.

3.4.9 Finally, digital exclusion amongst the older population is more widespread than among younger people. In addition, individuals may have access to IT equipment and support at work but not once they stop working. Even if individuals do use IT equipment at work they may be barred from using it for personal reasons. Digital exclusion will limit many people's ability to access useful, relevant guidance. As an example, throughout the Pension Wise document reference is made to websites where additional information can be found and it is only on the final page that telephone numbers for (some) organisations are provided.

3.4.10 We are also concerned that making it difficult for individuals to access HMRC refund claim forms such as P55 in paper copy will affect the digitally excluded. Many of those individuals who do have access to technology and use the internet will not be able to easily print out documents. Our colleagues at Tax Help for Older People had a case some months ago where HMRC's response to a request for a paper copy of a form was to suggest that the individual contact their local enquiry office; as the Committee will be aware the last of these offices closed in July 2014.

LITRG
3 September

Appendix 1

Requirements placed upon guidance providers, professional advisors and firms

The Financial Conduct Authority ("FCA") published a consultation paper in July 2014 (CP 14/11) and, as a result of the responses and other research, the FCA has published various documents setting out the responsibilities and obligations placed upon guidance providers, professional advisors and firms. A summary of these is set out below.

When individuals are investigating the options available to them with respect to their pension funds there are three opportunities for them to receive guidance or advice:

1. They are able to seek "guidance" on the options available to them and the associated risks from designated guidance providers, The Pensions Advisory Service and the Citizens Advice Bureau, collectively known as Pension Wise. Such guidance will be free of charge. Under the FCA's Designated Guidance Providers Instrument 2015 (FCA 2015/9)[1] the guidance provided should

    a. identify for the {individual} and provide them with information about the potential tax implications or debt obligations (FCA2015/9 clause 20f(iii)); and
    b. draw the {individual's} attention to the potential tax implications or debt obligations under standard 20(f)(iii) and refer them to support services, as appropriate (FCA2015/9 clause 21(d))

    In addition a *designated guidance provider* should have knowledge of *the tax treatment of pensions and income generally* (FCA 2015/9 clause 11(e)) and be aware of the individual's *entitlement to state benefits (current & future)* (FCA2015/9 part 3).

2. Individuals may also (and in some cases must) seek regulated advice from an independent professional advisor for which they will have to pay.

3. Finally, when an individual approaches a firm which manages his pension funds with a view to accessing these savings this firm is required to provide retirement risk warnings. [2] However, this requirement is waived if an adviser is managing the transaction on behalf of the individual or the firm has already provided risk warnings and believes that they are still appropriate. Firms will charge fees for acting upon the individual's wishes.

Firms or individuals providing services under options 2 and 3 need to have regard for the FCA's recommendations and comply with their Conduct of Business Sourcebook (COBS).[3] In

[1] http://media.fshandbook.info/Legislation/2015/FCA_2015_9.pdf
[2] FCA PS 15-04 clause 3.4 https://www.fca.org.uk/static/documents/policy-statements/ps15-04.pdf
[3] https://fshandbook.info/FS/html/FCA/COBS

their Policy Statement PS15/4 the FCA identified various risk factors which firms need to identify. These included:

- tax implications; and
- impact on means tested benefits.[1]

Upon identifying a risk factor a firm must provide a risk warning; the FCA does not prescribe the content or format of risk warnings.[2] Rule 19.4.7R[3] of COBS states:

> "If a *firm* receives an application from a *retail client* to access some or all of the proceeds of a *personal pension scheme*, *stakeholder pension scheme*, *FSAVC*, *retirement annuity* contract or *pension buy-out contract*, the *firm* must provide the *client* with a description of the tax implications before the *client* accesses those proceeds."

The FCA outlined their intention with respect to rule 19.4.7R in their Policy Statement PS14/17[4] issued in response to their consultation paper CP14/11:

> "Our intention is for firms to give a generic description of the tax implications of the option selected. However, in order that such communications are clear for the consumer, we encourage firms to illustrate the impact in a way that is relevant to the customer."

[1] FCA PS15-04 clauses 3.33 and 3.34

[2] FCA PS15-05 clause 3.38

[3] https://fshandbook.info/FS/html/FCA/COBS/19/4

[4] https://www.fca.org.uk/static/documents/policy-statements/ps14-17.pdf