THE CLIFTON GROUP

Investor in Customers® Gold 2018

Accelerating home ownership for first time buyers and increasing pensions engagement amongst the younger workforce

submitted to HMT by Clifton Asset Management Plc

First time homebuyers-solving the deposit savings problem and increasing pensions engagement at the same time.

Helping young people buy their own home and reducing dependency on the buy to let sector has long been a priority for successive governments.

At the same time governments have sought to increase young people's engagement with pensions and to increase the savings ratio in order to promote long term financial security and a reduced dependency on the state.

For many young people achieving both of these out of their take home salary is unrealistic and the deposit savings thus tend to take priority, leading to significantly diminished pension prospects in later life since, as we all know, an early entry into the pensions system is by far the best way to ensure an adequate retirement fund.

I believe that both of these issues can be addressed by combining them.

By way of background credentials I am chairman of Clifton Asset Management Plc. One of our core activities is the provision of SIPP and SSAS pension products to individuals who wish to do different and 'non-standard' things with their pension savings such as invest in their own business or make peer to peer investments. We have a long tradition of disruptive and innovative activity which includes the creation of the Alternative Business Funding platform, which has HMT designation under the mandatory bank referrals legislation and which is widely credited as being the inspiration for the legislation itself.

For now I am suggesting that this proposal is aimed at members of money purchase workplace pension schemes, not defined benefit type schemes, although it may be possible to extend its scope into that area.

The ability to do non-standard things with pensions has been around for a long time, and some groups, such as small business owners have been able to borrow from their pension pots under SSAS rules since 1979. My proposal is that, under strict conditions, we extend this capability to first time buyers up to a maximum, say, of forty thousand pounds. The numbers are compelling.

- It would take a young person between eight and ten years to amass a thirty thousand pound deposit by saving into an ISA at £250 per month from net income.
- The same fund value would be achieved through a net salary contribution of the same amount into a salary sacrifice employer sponsored workplace pension in less than fiveyears.
- The saver should be allowed to transfer the accumulated pension pot into a specially designed first time buyer SIPP.
- The SIPP provider facilitates a loan from the SIPP paid directly to the conveyancing solicitor to act as the individual's deposit. In this case thirty thousand pounds on an assumed 300k purchase price.
- Repayments to the pension are set at the same rate as the mortgage repayments and the same term. Repayments are collected by the mortgage provider and remitted to the SIPP provider in order to guarantee full repayment.
- The SIPP provider takes a second charge over the property in order to secure its loan.

- The individual continues membership of their workplace pension as they now have the pension 'habit'.
- Their homebuyers loan pension pot is repaid with interest over the term of the mortgage so there is no detriment to the eventual value of the pension fund and no adverse tax consequences.

Variations on this, such as an interest only arrangement linked to their eventual tax free cash entitlement are possible to address early stage affordability issues if needed. Either way, by taking a legal charge and linking repayments to the mortgage we can guarantee the outcome.

I believe that this policy would be a natural extension of the pension freedoms regime and by using the efficiencies of pension saving to increase home ownership amongst young people we would have significantly advanced the prosperity agenda since pension membership and home ownership are the two main planks of an individual's long term financial security.

Based on my understanding of how these things work I don't believe that this change requires primary legislation, it could be introduced as policy by the Chancellor in the same way as the pension freedoms regime. I also believe that it would be tremendously popular amongst young people, a constituency that the current government would very much like to impact. It would be equally popular with plenty of parents too, since it would significantly reduce the burden and pressures of being 'the bank of mum and dad'.

The scheme should be administered by HMT designated SIPP providers who can demonstrate that they have the back office capabilities and team experience to manage an extensive loan book. There are at least a dozen such providers currently capable of doing this, all of whom would be highly motivated to participate. This creates quality competition in the space as well.

Of course there are always losers, and in this case a rapid increase in home ownership amongst the young may take some of the shine off the buy to let sector.

Table A – shows the total contribution to various savings vehicles at a corresponding net cost to the individual of £250.

	ISA	Personal Pension	Workplace pension	Workplace pension with salary sacrifice
Gross employer	£0.00	£0.00	£41.67	£460.05
Gross employee	£250.00	£312.50	£312.50	£0.00
Total	£250.00	£312.50	£354.17	£460.05
Net cost to individual	£250.00	£250.00	£250.00	£250.00

The first column shows the gross contribution that would apply to an ISA based on a cost to the individual of £250.00.

The second column illustrates the gross contribution that would apply to a standard Personal Pension based on a cost to the individual of £250.00.

The third column illustrates the gross contribution that would apply to an individual in a standard workplace pension scheme, based on a salary of £25,000.

The fourth column illustrates the gross contribution that would apply to an individual in a standard workplace pension that offers salary sacrifice (and includes the full NI rebate on both employer and employee contributions), based on a salary of £25,000.

Table B – shows the projected funds over a period of 5 and 10 years assuming that the respective payments are paid monthly.

	ISA	Personal Pension	Workplace pension	Workplace pension with salary sacrifice
5 years	£17,300	£21,700	£25,700	£31,900
10 years	£39,200	£49,000	£58,400	£72,200

Notes

- It is assumed that all payments increase by 5% pa.
- The projections do not take into account any associated investment costs.
- The minimum employer contribution to a workplace pension is 2% from April 2018 and increases to 3% from April 2019.
- It is assumed that there are no salary increases for the duration of the workplace pension.

After 5 years, a sizeable pot would have accumulated which could enable an individual to draw a loan from their SIPP. Where the interest rate charged on the loan is the same as the assumed growth rate of the pension fund, the projected funds will be unchanged as can be illustrated below:

The following tables show the projected funds over 5 and 30 years, with a contribution rate of £460.05pm (see table A) for the duration of the period.

Table C – assumes a loan of £30,000 is taken at a rate of 5%pa on a repayment basis:

	Fund value assuming loan drawdown of £30,000 after 5 years	**Fund value assuming no loan drawdown**
5 years	£31,900	£31,900
30 years	£385,000	£385,000

Notes

- It is assumed that all payments increase by 5% pa.
- The projections do not take into account any associated investment costs.
- It is assumed that there are no salary increases for the duration of the workplace pension.
- The loan is payable in equal capital and interest instalments at a rate of 5% for a 25 year term. The monthly payments equate to £175.38.

Table D – assumes a loan of £30,000 is taken at a rate of 5%pa on an interest only basis:

	Fund value assuming loan drawdown of £30,000 after 5 years	**Fund value assuming no loan drawdown**
5 years	£31,900	£31,900
30 years	£355,000	£385,000

Again, despite a lump sum being taken from the fund after 5 years, the interest payment back to the SIPP means that there is no difference to the outcome of the fund after the expiry of the loan term (other than the loan capital).

Notes

- It is assumed that all payments increase by 5% pa.
- The projections do not take into account any associated investment costs.
- It is assumed that there are no salary increases for the duration of the workplace pension.
- The loan is interest only at a rate of 5% for a 25 year term. The monthly payments equate to £125.00.
- The loan capital remains outstanding at the end of the term.

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