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By email to statisticsenquiries@hmrc.gov.uk
To whom it may concern

Consultation on changes to HMRC statistics publications

Private pension statistics

I refer to your release of 24 October 2022 noting the consultation on the HMRC statistics publications (and thank you for the extension on the period for response, while we have been thinking about the latest relevant release of statistics).

I am writing on behalf of the Association of Consulting Actuaries with comments focussed on the Private pension statistics pages (mostly recently updated September 2022) - as supplemented by and contributing to the forecast document on broader tax reliefs, most recently issued in January 2023 here Non-structural tax reliefs - GOV.UK (www.gov.uk) . We had no material comment on HMRC's proposed limited changes to some of the statistics in this area as announced in the 24 October 2022 release, but we are responding to your invitation for comments on the programme in general. In particular, our concern is around the way limitations in estimating pension tax relief are communicated to users.

Pensions tax relief is one of the five largest areas of tax relief and is important both to the economy and to the population. It is probably common ground that it is therefore important that policy makers have useful, relevant and reliable statistics for decision-making, that they understand the nature of the statistics they are given and understand how the statistics should be read. The same is true of external users.

We appreciate that a huge amount of work is put into compiling these statistics, and that pensions is a difficult area on which to place a cost. In particular there are challenges in getting relevant source data (and in some areas, with direct source data being unavailable, the data have to be substituted by proxies). There is also a range of views on the best way to put an amount on the value of a defined benefit promise (and differences between funded promises and (typically public sector) unfunded promises), and how best to value past and ongoing elements. The different views will each have their advantages and disadvantages in terms of the information and steer they provide.

1 Inherent uncertainty in the pension tax relief statistics is not always clearly and prominently communicated to users

Our concern is that the statistics for the cost of tax relief on private pensions is, for good and understandable reasons, difficult to quantify accurately but the size of the relief is sufficiently large to be of interest to politicians, policy-makers, those lobbying for policies, the public and the media.

The uncertainty inherent in compiling the statistics causes them to be subject to regular and sometimes material revision and the statisticians compiling them know both the uncertainty in the numbers and that the values can be significantly affected by assumptions made in compiling them. However, these known and important imperfections, which we acknowledge are almost impossible to avoid, are not always made as clear to users as they could be.
This is in extension to the very important point that the "costs" are not potential gains to the exchequer were the reliefs to be removed – we comment further on this in section 3.

The consequence is that these statistics, carrying the National Statistics quality assurance badge, are treated by most users as definitive, accurate facts – when they are a best attempt at making difficult estimates which still carry significant uncertainty and nuance.

As an association of professional actuaries (and within our member firms) there are frequently comments made noting concerns that these published statistics have been (or could be) used to highlight the cost of pensions tax relief in a way that is misleading, sometimes inadvertently and sometimes possibly to lobby for a particular policy position. While the ACA is strictly politically neutral, we are keen to see well-informed and accurate debate in this area. We would not wish to see any misconstrued data being used, however inadvertently, to form the basis of future policy proposals.

In that context, our headline comment is that we believe that all stated estimates on pensions tax relief should have a very visible health warning each time they are stated, whether in HMRC documents or ministerial policy statements or documents. We know that HMRC statisticians and the Office for National Statistics are well aware of the uncertainties underlying the pension tax relief statistics, and that it is set out in the footnotes to the tables, but our experience is that most users never read that far.

Furthermore, we think that, given the very big differences, there would be much merit in more emphasis being put on the breakdown between DC provision, DB private sector and DB public sector, than on the composite figure - but again there should be appropriate health warnings given to each element. We would be happy to discuss how this could be approached.

Areas in which the presentation of the statistics might be improved are:

- more acknowledgement that some figures are not straight facts but are based on chosen methodologies;
- more transparency about the methodologies used – so that, where different users disagree, there can be informed open discussion – see the Appendix for a particular example (how tax relief is measured on deficit reduction contributions (**DRCs**) where a defined benefits pension scheme has a deficit to be funded); and
- more indication of the sensitivity of the costings to choices of methodology or assumptions.

Suggested improvements in the summary analyses might be:

- more analysis of underlying trends and stronger link to external events and policy actions;
- more reminders about the unreliability (currently these are hidden in footnotes); and
- care about spuriously "accurate" statements, for example the split of how the tax relief is shared between different levels of earners.

We note that the "McCloud remedy" is shortly to be implemented and will lead to revised reading of past benefits, and presumably further upward revision of numbers. It will be essential that there is transparency of methodology here, or else this could lead to even more risk of misreading of the statistics.

2 Correcting/updating statistics

A warning appears regularly in the footnotes to the September detailed statistics (including the September 2022 release highlighted above, in the notes to Table 6), that the [tax relief estimated] '*costs are subject to large revisions and have a particularly wide margin of error'.* (The warning is rather more buried in the general reliefs release, appearing specifically in the December 2021 release, but in the January 2023 release cited above it is only referred to by link back.)

One example of a significant change in numbers occurred with the September 2022 release. Table 6 within Private pension statistics had figures for 2020-21 very different to those for the same tax year provisionally released in December 2021 (figures which we used in our September submission to the Treasury Select Committee on pensions tax relief). The change was from £42.7bn to £48.2 bn, attributed to improvement in methodology (with some but limited explanation). The 2019-20 headline figures were correspondingly revised at the same time (from £41.8bn to £44.4bn) and the headline figures for years back to 2017/18 were correspondingly revised very recently released in January 2023.

Of course, improvements to statistics are a good thing, but without underlying detail being shown, changed numbers for a tax year mean that tracking back to underlying trends (e.g. between different types of benefit) is impossible. In addition, past commentary that has been issued based on earlier statistics might not remain valid.

3 Compilation of statistics/methodology

It has been pointed out on several occasions that tax relief statistics do not correctly represent the opportunity cost for saving. Indeed, two warnings constantly appear in the body of the releases of the statistics, even if a number of readers do not seem to notice them. We noted one above, but in addition, in the overall relief statistics (for example those published earlier this month in **Error! Hyperlink reference not valid.** there is a warning:
"*these estimates do not represent the gain to the exchequer should a relief be abolished because of behavioural effects, interactions between reliefs and wider economic impacts of withdrawing relief ...",* and later *"These figures should be regarded as broad estimates, as the loss of revenue from a tax relief cannot be directly observed so the estimates are often based on assumptions."*

This is a really essential point for readers to understand. We think it should be repeated in headline form within all the pensions tax relief documents. As far as we can see, in the pages Private pension statistics it appears as a small note under a table but we suggest it is incorporated elsewhere in the September releases and particularly in the Commentary.

We would also argue that there are methodology reasons why the estimates should not be used for such a purpose and need to be used with huge care. We give two examples (one specific to the DB private sector) in the Appendix.

We hope you find our comments useful. We would be happy to discuss this matter further if you wish. If so, please contact Jillian Pegrum on 01252 768175 or at jillian.pegrum@aon.com, or me on 020 7432 6621 or at karen.goldschmidt@lcp.uk.com.

Yours sincerely

Karen Goldschmidt FIA

Chair of the ACA Pensions Tax committee
On behalf of the Association of Consulting Actuaries Limited

Appendix

Examples of concerns about compilation, methodology, and transparency

Deficit Reduction Contributions to private sector DB pension schemes

It is pointed out that tax relief statistics do not reasonably represent the opportunity cost for the government to make changes to save costs. A particular example is the treatment of Deficit Reduction Contributions (**DRCs**) for private sector defined benefit pensions savings. DRCs are made by employers to address funding shortfalls in defined benefit pension schemes needed to deliver obligations accrued to date across the membership, in respect of current active members but also those who have left service and who are pensioners or deferred pensioners.

- HMRC's cost estimates include income tax and National Insurance relief in respect of DRCs. It seems unlikely that HMRC could ever charge members the taxes arising on these; so there is some argument that this should be excluded from a figure that might be used for policy making.

- If one accepts the inclusion of DRCs, then there is the question of how to attribute an appropriate amount of income tax relief to them. Our understanding is that HMRC treats the DRCs paid into any particular funded private DB scheme as if it were shared between just its active membership, with the marginal tax rates that would apply. For example, if a scheme has 100 pensioners and 1 active member then any DRC (to fund a deficit that had arisen among other things from the pensioners' life expectancies increasing) would be deemed to be paid exclusively for, and would be attributed to, the one active member. If there are no active members, it does a similar respreading but across the active members of all other private sector schemes. All of the above is likely to misrepresent (and probably overstate) the tax bands involved.

- HMRC gave the explanation of the methodology in its September 2021 release. For the September 2022 release, there is a headline statement of some changes in methodologies but with little detail. Where DRCs are mentioned in a later section, instead of the 2021 detail, there is a comment referring to "an estimated average marginal tax rate for a comparable group". Is this a change of approach or less information about the (flawed) approach noted above?[1]

Using this approach makes it impossible to analyse the statistics for pension contributions properly; and such figures are often used by politicians to make comments about the overall cost of pensions tax relief. We understand that a different or modified approach applies to public sector schemes, given their largely unfunded status. These differences increase the complexity for interested users to understand how the results are derived.

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[1] [ARCHIVED CONTENT] Background and Methodology - GOV.UK (nationalarchives.gov.uk) with as at date 28.10.2021 issued alongside statistics released in September 2021:issued within [ARCHIVED CONTENT] Personal and stakeholder pensions statistics – GOV.UK (nationalarchives.gov.uk) with as at date 28.10.2021: *"Employer contributions and rates are taken at face value from ASHE, in the case of Defined Benefit schemes, rates from ASHE are used to proxy the value of the pension promise made by employers to their employees. HMRC also use available years from MQ5 (MQ5: investment by insurance companies, pensions funds and trusts QMI - Office for National Statistics) (link) published by the ONS to give estimates of contributions needed to fund pension deficits (DRCs) in the private sector. For funded DB schemes HMRC's modelling allocates DRCs to members in private DB schemes based on the weighting of their employer contributions, therefore a member with larger employer contributions will be allocated a larger value of DRCs. Employer contributions are then treated in a member's income stack 'sitting' above their individual contributions. Estimated DRCs are split among active members of private DB schemes. A closed DB scheme with no active members will not be included in the modelling, their share of estimated DRCs will be included in the ONS' MQ5 estimate and will be allocated across active members of private DB schemes in HMRC's modelling."*

In the 2022 equivalent Background and methodology - GOV.UK (www.gov.uk) the explanatory notes simply say "*DRCs are identified using the FSPS, and an average income tax rate is applied. … Contributions may 'straddle' tax bands and therefore not all be relievable at the same rate – this is modelled in Table 6 where total income or pay are available at an individual or employee level. Where total income or pay is not available on an individual or employee level, such as for DRCs, an estimated average marginal tax rate for a comparable group is used."*

Tax on payments

The statistics count the cost of current tax relief on contributions for today's employees and then nets off the tax receipts from current pensions (and flexible withdrawals) for today's pensioners. The cost of tax relief on the investment income of pension schemes sits somewhere between these two extremes, as it relates to contributions paid in the past that are not currently being used to pay out benefits.

The comparison of tax relief on current contributions with tax received on current pension payments has the effect of overstating the cost of tax relief by comparing the current workforce's relief (which is growing due to the increased membership of schemes) against the receipt of tax from a smaller pensioner population. We realise that it would be very difficult to correctly balance the cost of tax relief and income tax received between the relevant cohorts, but - even with caveats present - this can easily be misinterpreted.

Members of the ACA are all qualified actuaries – mainly Fellows of the Institute and Faculty of Actuaries. All actuarial advice given by our members is subject to the Actuaries' Code. Members provide advice to thousands of employers and pension schemes - with total assets exceeding £1 trillion - including most of the country's largest schemes – and increasingly consulting actuaries are now involved in a wide range of additional areas.