



By Product of Tax Increases.

Oh dear! Oh dear! The proposed national scheme of Personal Pension Accounts (that will be introduced in 2012) is aimed at people on moderate to low earnings. It has already been decided that there will be auto-enrolment into the scheme, which these days is increasingly referred to as 'soft compulsion', is a process that will ensure millions of people in this 'target market' will begin to save for a pension in a national money-purchase occupational pension scheme.

That scheme has the potential to be the largest private sector pension scheme in the world and as such will be light on the advice side and therefore high on the trust side. For millions I'd guess it will be a leap of faith.

There are problems with that approach, of course, but there are problems everywhere in life if you look for them. But the leap of faith those who rely on trust will need to make when they commit to this lifetime savings plan has just got a bit wider.

The chasm was already fairly wide anyway; for those not saving significant amounts of money will probably end up with the worst of all worlds. A very small pension that precludes them from receiving any of the multitude of means tested benefits; and the increases in expected longevity cutting the real value of the proposed 8% contribution not helping either.

But we've now got a new tax system following last week's Budget.

The reduction in the basic rate of tax from 22% to 20% leads to good headlines, but a poor reality for those on low earnings. The fact is low earners are likely to end up paying more tax under the new system as the reduction in the basic rate fails to compensate for the loss of the 10% starting rate. For many in the 'target market' that will mean less take-home pay, just as paying the softly-compelled 4% pension contribution will.

At the same time, the help that many people who save in pensions get from the taxman will diminish as a result of the cut in the basic rate of tax. This is yet another chasm-widening issue for the lower-paid pension investor. Under the present system every £78 invested is grossed-up to £100 with tax relief. In future each grossed-up £100 in a pension pot will require an investment of £80.

An interesting question; just how wide does this chasm have to be before people start to think twice about making the leap of faith?

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