HELP TO SAVE

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THE CENTRE FOR
SOCIAL
JUSTICE

In his Life Chances speech on 11 January 2016, the Prime Minister said:[1]

> 'We'll also do more to help people save – and help build families' financial resilience. Those with no savings at all have no buffer – no shock absorber – for when unexpected events hit. … So I can announce today that we intend to bring forward a "help to save'"scheme to encourage those on low incomes to build up a rainy day fund, and full details of this scheme will be announced in the Budget.'

This short paper, written after a Centre for Social Justice (CSJ) roundtable with leading thinkers in this area, is intended to help inform the Government's thinking as it prepares a 'Help to Save' scheme for people on low incomes.

Background

The need for a savings scheme

There is a sizeable body of evidence showing that too many people in the UK have few or no savings.

- 24 per cent of working-age people never or rarely save money – around a quarter say they currently have no savings;[2]
- Four in 10 adults have less than £500 in savings;[3]
- 21 million do not have even £500 in savings to cover unexpected bills like replacing the fridge or mending the car;[4]
- 13 million people in the UK lack the savings to keep up with essential bills for just one month if their income dropped by a quarter;[5]
- This problem is most acute among low- and middle-income households: 42 per cent of people earning less than £15,000 per year do not have a month's savings and 80 per cent of the poorest households do not save regularly.[6, 7]

This lack of savings exposes families to income shocks and the risk of problem debt. As the CSJ's work has repeatedly shown, the stress of managing tight finances and dealing with creditors, as well as the stigma associated with problem debt, can lead to mental health conditions, family breakdown, addiction, worklessness and crime. Many of those negative

1 Rt Hon David Cameron MP, *Prime Minister's speech on life chances*, 11 January 2016 [accessed via https://www.gov.uk/government/speeches/prime-ministers-speech-on-life-chances (07/03/16)]

2 The Money Advice Service, Press Release, *Media comment: IFS report on household wealth and attitudes to savings*,19 November 2015 [accessed via https://www.moneyadviceservice.org.uk/en/corporate/media-comment--ifs-report-on-household-wealth-and-attitudes-to-savings (07/03/16)]

3 The Money Advice Service, Press Release, *Four out of 10 adults are not in control of their finances – new strategy launched to improve UK's financial capability*, 28 October 2015 [accessed via https://www.moneyadviceservice.org.uk/en/corporate/four-out-of-10-adults-are-not-in-control-of-their-finances-new-strategy-launched-to-improve-uks-financial-capability (07/03/16)]

4 The Money Advice Service, Press Release, *Four out of 10 adults are not in control of their finances – new strategy launched to improve UK's financial capability*, 28 October 2015 [accessed via https://www.moneyadviceservice.org.uk/en/corporate/four-out-of-10-adults-are-not-in-control-of-their-finances-new-strategy-launched-to-improve-uks-financial-capability (07/03/16)]

5 StepChange, *Life on the edge: Towards more resilient family finances*, London: StepChange, 2014 [accessed via https://www.stepchange.org/Portals/0/StepChangeLifeontheEdgereport.pdf (07/03/16)]

6 StepChange, *An action plan on problem debt* [accessed via http://www.stepchange.org/Mediacentre/Researchandreports/ProblemDebtActionPlan.aspx (07/03/16)]

7 Personal Finance Research Centre, *Towards a nation of savers*, Bristol: Personal Finance Research Centre, 2011

outcomes are interrelated and can also drive problem debt, trapping people in a 'vicious cycle' where the consequences of debt make it harder for people to extract themselves from it.

Previous government attempts to offer savings schemes

Over the past 20 years there have been a number of government-backed schemes to encourage savings. These have included:

- Child Trust Funds;
- The Savings Gateway.

Both of these were abolished by the Coalition Government in 2010. The Savings Gateway provided a targeted attempt to help low earners and benefit claimants save by offering financial incentives to those who put money into the scheme. Whilst the evaluations showed that incentives were effective in encouraging people to put money aside, it was also clear that there was a problem in helping the poorest – i.e. those most in need of the scheme – find money to save.[8]

As one member of the roundtable pointed out, people earning £270 a week are likely to be only able to save 80p a week once they have covered their basic costs.[9] This means that in order to cover the cost of a new washing machine at £140, it would take 175 weeks (or three and a third years) to save up enough for this basic household product.[10] Even if the Government match funded these savings it would take over 20 months to reach the right level. Consequently, any new savings scheme should, ideally, look to identify new money with which they can save.

Key themes

The CSJ heard that there were advantages to:

- Encouraging people to save by creating financial incentives such as rewards or prizes;
- Making it easier for people to save by, for example, creating automatic savings initiatives;
- Helping people to plan for the different income cycles that they face:
  - Unexpected income shocks (e.g. broken washing machine);
  - Expected income shocks (e.g. Christmas, car tax etc.).

8 See evaluations at HM Treasury Saving Gateway [accessed via: http://webarchive.nationalarchives.gov.uk/20130129110402/http://www.hm-treasury.gov.uk/documents/financial_services/savings/topics_savings_gateway.cfm (07/03/16)]

9 Office for National Statistics, *Family Spending: 2015 Reference tables: Table 3.1*, London: Office for National Statistics, 2015 [accessed via: http://www.ons.gov.uk/peoplepopulationandcommunity/personalandhouseholdfinances/incomeandwealth/compendium/familyspending/2015/familyspending2015referencetables (07/03/16)]

10 Cheapest machine available online on 17/02/16

Prize-linked savings

There was an acknowledgement that prize-linked savings schemes had considerable potential, as has been shown by the experience of programmes in Michigan, USA (Save to Win),[11] South Africa (Million a Month),[12] and in the UK with premium bonds. Prize-linked savings have a strong track record of encouraging people to put money aside – even though they often deliver lower returns than mainstream savings products.[13]

Enhanced interest rates

Enhanced interest rates have been used in pensioner bonds in the UK to encourage saving. The original Savings Gateway offered something similar by match funding (or partially match funding) the amount put in by the saver. By using government money to subsidise savings, it is possible to offer the saver a guaranteed cash incentive to put money aside. The downside is that such schemes can quickly become expensive and offer most reward to those most able to save.

Auto-enrolment/opt-out savings

The CSJ heard that a potentially powerful way to incentivise saving amongst those in work would be to create an employer-based auto-enrolment savings scheme. The use of auto-enrolment to encourage people to save for their pensions is widely seen as a considerable success with large increases in the number of people paying contributions.[14]

As pensions are a form of long-term saving the same logic and evidence is applicable to developing a new system of auto-enrolment in employer based short-term saving schemes.

Many firms already operate such schemes to help employees plan for future spending and deal with financial emergencies. These include:

- **Save as You Earn (SAYE):** a 3–5 year scheme requiring monthly savings that are then topped up with a tax-free bonus at the end;
- **Share Incentive Plans (SIPs):** schemes to allow employees to buy shares in their employer's company with a variety of tax incentives and other bonuses;
- **Workplace ISAs:** as they are negotiated in bulk by the employer these ISAs offer better terms and interest rates, with some employers offering payroll deductions to make saving easier.

By utilising the auto-enrolment technology developed for pensions, it should be possible for government to provide a means of offering workers access to a savings scheme which could divert funds to any number of savings vehicles, such as bank accounts, credit unions, bonds etc.

11 Save To Win [accessed via: http://www.savetowin.org (07/03/16)]
12 Kellogg Insight, *Using the lure of a lottery to spur savings*, 2 March 2015 [accessed via http://insight.kellogg.northwestern.edu/article/using-the-lure-of-a-lottery-to-spur-savings (07/03/16)]
13 Money Saving Expert, *Premium Bonds are they worth it?*, February 2016 [accessed via http://www.moneysavingexpert.com/savings/premium-bonds (07/03/16)]
14 Office for National Statistics, *Pension short stories: Employees eligible for automatic enrolment: contributions to workplace pensions,* 2005 to 2014, London: Office for National Statistics, 2015 [accessed via: http://www.ons.gov.uk/ons/rel/pensions/pensions-short-stories/employees-eligible-for-automatic-enrolment--contributions-to-workplace-pensions--2005---2014/art-employees-eligible-for-automatic-enrolment--contributions-to-workplace-pensions.html (07/03/16)]

A new savings scheme

On the evidence the CSJ has been presented, there would be merit in developing a savings scheme which:

- Made it easy for low-income families to save;
- Shared efficiency savings between the Government and the saver;
- Offered a 'prize' element.

Scheme 1: A simple savings scheme

Using auto-enrolment procedures the Government could set up an opt-out savings system that would encourage low earners to put aside a proportion of their salary into a savings account. This would partially match fund savings made by the individual until they had reached a certain level, say, £150.

Depending on the level of the subsidy, this might allow someone to save £100 of their own money over a year (£1.92 a week) and receive £50 (96p a week). If the scheme was open to all those exempt from income tax, it would, in effect, amount to a £50 payment to each of them.

As discussed above, it might be difficult in practice for many low earners to put aside the £1.92 necessary to save for a washing machine over the year. For many it would require two or more years' savings.

Scheme 2: A savings scheme from efficiency savings

Ongoing welfare reform provides a unique opportunity to introduce a more radical approach, which would provide low-income households with the ability to accrue savings without needing to find need new money from tight budgets.

We suggest that this could be achieved by replacing contribution-based Jobseeker's Allowance (JSA) and contributory Employment and Support Allowance (ESA) with a better system. Currently, when a person falls out of work, they can claim out-of-work benefits in one of two ways:[15]

- Contribution-based JSA or contributory ESA, where someone has made sufficient National Insurance (NI) contributions in recent years. The claim that can be made is time-limited for six months and a year respectively;
- Income-based JSA or ESA, which are means tested, and cannot be claimed by those with savings over £16,000.

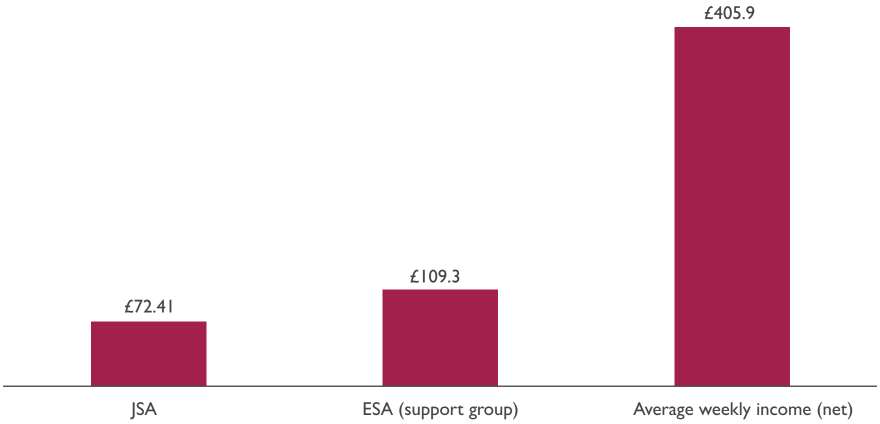
This means that there is a kind of 'insurance' element to NI: that even if someone has savings, they will still get something out of the system if they have been paying their NI contributions.

15 HM Government, *Jobseeker's Allowance (JSA)* [accessed via: https://www.gov.uk/jobseekers-allowance/overview (08/03/16)]; HM Government, Employment and Support Allowance (ESA) [accessed via: https://www.gov.uk/employment-support-allowance/overview (08/03/16)]

However, this system also has significant disadvantages.

First, the level of contribution-based JSA or contributory ESA is significantly less than a working income, which means that when someone is made redundant or becomes too ill to work they will receive a considerable, sudden income shock. For instance, someone who had been on a weekly income of £406 (the national average after tax) could find themselves in receipt of a quarter of their original wages, even though they might have paid their NI contributions throughout their life.

Figure 1: Weekly income of average earner[16]



It should be noted that the figures above do not include other benefits that can be claimed when someone becomes unemployed – notably Housing Benefit in the case of renters.

A second drawback is that those on lower incomes, who would qualify for a full income-related JSA or ESA anyway, do not benefit from this system. For instance, someone may earn £12,000 a year and pay into the system for 30 years. But if they have no savings when they lose their job then they may be no better off claiming the contribution-based JSA since they may also eligible for full income-based JSA.

Third, contribution-based JSA or contributory ESA do not fit within the framework of Universal Credit, which is purely designed as an income-related benefit system so that there is a gradual taper-off of benefits as people move into work and increase earnings, thus eliminating work disincentives.

If contribution-based JSA and contributory ESA were abolished those on lower incomes would still be able to claim income-based benefits. Meanwhile, it would create substantial

16 Figures obtained from Age UK, *Employment and Support Allowance* [accessed via: http://www.ageuk.org.uk/money-matters/claiming-benefits/employment-support-allowance/what-you-get-on-employment-and-support-allowance/ (09/03/16)]; Entitled To [accessed via: http://www.entitledto.co.uk/ (09/03/16)]; Listen to Taxman [accessed via: http://www.listentotaxman.com/26500 (09/03/16)]

savings for the Treasury from those with sufficient means to not be eligible for income-based JSA or ESA. Such savings could be used to kick-start a new scheme for employment insurance to replace contributory benefits for this group.

For instance, the savings could be used to raise the threshold at which NI is paid from £8,600 per year to £10,000. This would save households earning over the £10,000 threshold £240 per year.

At the same time, the Government could introduce a workplace auto-enrolment scheme for a new national Rainy Day Guarantee. For a premium of 0.5 per cent of gross salary – £5 per month for someone earning £12,500 a year – this could offer better contributory salary protection than that currently afforded through NI.[17] In other words, if someone lost their job, this system would pay out better than JSA or ESA, even though people were paying less in.

It is worth noting that there will be some low-income people who, if they lost their job, would be able to claim both their Rainy Day Guarantee and income-based JSA – such as in case cited above of someone who has been earning £12,000 for 30 years but has few savings.

Rainy Day Guarantee

- Premium of up to 0.5 per cent of gross income;
- Delivered by providers of auto-enrolled workplace products;
- It pays out a percentage of the contributor's salary for a defined period should someone lose their job through redundancy or ill health;
- Covers up to £42,000 of income;
- Integrates with Universal Credit.

The Rainy Day Guarantee scheme would replace the 'insurance' element of contributory benefits, while still leaving an average earner nearly £2.60 a week better-off than under the old system.

People could be encouraged to save this extra income through auto-enrolment of 1.5 per cent of gross income into a Rainy Day Savings Account. It would be possible to use credit unions as a place of deposit for these funds – strengthening the sector and so increasing the number of low-income savers and borrowers they can help.

Introducing these two new schemes (Rainy Day Guarantee and Rainy Day Savings) at the same time as raising the NI threshold, would be a further nudge (along with auto-enrolment) for people to make use of these schemes, as people would feel the benefit of the raising of NI thresholds at the same time as they have their money taken out of their account through

17 Calculations in this section by L&G, available on request

auto-enrolment. Crucially, such a scheme would also mean an individuals net pay (for lower earners) would not reduce as a result of this change.

A further element could be introduced to the Rainy Day Savings Account Scheme to encourage low-income people to keep their savings in their account, and to boost those savings. This might, for example, amount to 'Christmas bonuses' for those who had saved above a certain limit or not made any withdrawals that year. The level of bonus could be tapered from the full amount for those not earning enough to pay income tax (currently £10,600) to, for example, those earning the national average (£26,500) so as not to create work disincentives. These bonuses might be funded through some of the savings from abolishing contribution-based JSA and contributory ESA mentioned above, or through a separate fund.

Such a scheme has much to recommend it. Because it finds new money through efficiency savings it effectively allows government to let low-income earners keep more of their money and use that as savings.

In addition, the CSJ heard that earners might be less likely to enter into savings schemes if they felt that it was only for 'poor people'. The scheme outlined here, being entirely automatic, would have the added advantage of not requiring anyone to self-identify as 'poor' – low-income earners would simply, automatically, equip themselves with the tools of financial resilience.

Scheme 3: Premium bonds

The CSJ repeatedly heard that prizes are an excellent incentive to savings. This has been proved by the success in the UK of premium bonds. Premium bonds are a lottery bond offered by the UK Government and the National Savings and Investment Agency. Bonds can be bought in units of £10 after the first £100, with a value of £1 per bond and a minimum purchase of 100 bonds (or 50 bonds when paying by standing order) and offer a 1/26,000 chance of winning.[18] The scheme has been hugely successful in encouraging people to save – about one in three Britons saves in this way.[19]

However, the minimum purchase amount means that the scheme is effectively inaccessible to anyone who cannot afford a one-off payment of £100 or a regular payment of £50 and, consequently, it excludes lower income families. The Government could adjust this minimum payment and allow, for example, anyone who was exempt from paying income tax to buy premium bonds in smaller quantities. This might mean that someone could buy £5 of premium bonds every month and so, overtime, acquire savings with the possibility of this money being increased through winnings. Access would also be key, so being available via the Post-Office and supermarkets would support take-up.

18 National Savings and Investments, *Premium Bonds Facts and Figures* [accessed via http://www.nsandi.com/premium-bonds (07/03/16)]

19 Lobe S and Hölzl A, *Why are British Premium Bonds so Successful? The Effect of Saving With a Thrill*, 2007 [accessed via http://papers.ssrn.com/sol3/papers.cfm?abstract_id=992794 (7/3/16)]

Whilst this scheme alone would probably not allow many low earners to build up high levels of savings, it might encourage more to start saving. It would also be possible to combine this with the previous scheme and give savers the option of placing their savings directly into premium bonds.

Further issues

A difficult issue is how accessible any saved pot should be to the saver. Ultimately the perfect system would discourage people from withdrawing their money unless they were in genuine need but allow them to do so in a timely fashion when they were.

Under an auto-enrolment scheme it would be worth working with the Behavioural Insights Team to see how friction could be built into the system so as to discourage but not prevent withdrawals. This might include considering the effect of bonus schemes (e.g. £50 bonus each Christmas if you have not withdrawn funds) or a 24-hour withdrawal time that would add a degree of inconvenience without making it critical.

Conclusions

There would appear to be considerable advantages to using auto-enrolment infrastructure to create a savings platform.

All of these ideas would need to be tested and fine-tuned in order to see how they would best help low-income workers to save to levels that would protect them from income shocks and problem debt.

There are a number of additional factors that could help to increase the financial resilience of low earners, these include, alongside employment and career progression:

- Improved access to insurance products;
- Better options for lower cost credit and financial services that meet their specific needs.[20]

20 As set out in Centre for Social Justice, *Restoring the Balance*, London: Centre for Social Justice, 2014 [accessed via http://www.centreforsocialjustice.org.uk/publications/restoring-the-balance-tackling-problem-debt (07/03/16)]

In a sense, both these issues are addressed by Scheme 2, detailed above. The reform of contributory benefits has the potential to offer improved salary insurance, increasing payments but reducing premiums. Likewise the scheme would potentially create capital which individuals could use to leverage credit at lower rates.

By using efficiency savings to build a new generation of savers, the Government could potentially offer a cost-free means of helping low earners to acquire savings and so protection against problem debt and all the difficulties that accompany it.

About this report

On 8 February 2016, the CSJ convened a roundtable to discuss the issue of savings for low-income people with a select group of stakeholders who work within this area of policy. This report is the outcome of that discussion.

We are extremely grateful to all those organisation that made this work possible, which include:

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- JP Morgan
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