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Written Evidence to the Treasury Committee's Call for Evidence on Lifetime ISAs

About the Building Societies Association

The Building Societies Association (BSA) represents all 42 UK building societies, including both mutual-owned banks, as well as 7 of the largest credit unions. Building societies have total assets of almost £525 billion and, together with their subsidiaries, hold residential mortgages of over £395 billion, 24% of the total outstanding in the UK. They also hold £399 billion in retail deposits, accounting for 19% of all such deposits in the UK. Building societies account for 40% of all cash ISA balances, and four societies currently provide cash Lifetime ISAs. With all their headquarters outside London, building societies employ around 52,300 full- and part-time staff. In addition to digital services, they operate through approximately 1,300 branches, holding a 30% share of branches across the UK.

Executive summary

The BSA welcomes the opportunity to provide evidence to the Treasury Committee's Inquiry into the Lifetime ISA (LISA). We support the Government's aims for the LISA: to help first-time buyers save for a deposit and encourage long-term saving for retirement. The challenges many people face to buy their first property or enter retirement with a sufficient financial buffer have been exacerbated by the UK's cost-of-living crisis and are well understood.

We welcome initiatives that help people overcome these challenges whilst encouraging a nation of savers; it is our view that savings vehicles that provide a financial incentive for long-term saving can achieve this and make a meaningful impact on society.

However, the way the LISA operates today is not effective: its existing rules are unfairly punitive, its limits too restrictive, and its terms too complex to meet its objectives.

Recommendations for reform:

1. **Reduce the withdrawal penalty to 20%.** The LISA 25% withdrawal charge is unfair and can result in well-intentioned savers receiving less than they put in: they can currently be penalised if they:

    a. need to access their savings before they are able to purchase their first property, or

    b. withdraw their money to purchase a more expensive property than the LISA limits allow – despite initially using the LISA scheme as it was intended. Reducing the withdrawal penalty to 20% would allow people to access their own money if they need to, forfeiting the Government bonus but not their own hard-earned savings. This was introduced, on a temporary basis, in 2020/21 during Covid, which demonstrates that it can be done.

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2. **Increase the property price cap.** The LISA's £450,000 property price threshold has remained the same since 2017 despite a rise in house prices of at least 30%[1], which is now preventing people from buying their first home within the limit. This threshold should be increased to at least £585,000 to reflect the change in average house prices since LISAs were introduced.

3. **Raise and equalise the Help to Buy ISA threshold in line with LISA.** The Help to Buy ISA (HTB ISA) was created for first-time buyers to purchase a property but has two different property price thresholds – £450,000 for London and £250,000 elsewhere – whereas the LISA's threshold is £450,000 everywhere. The HTB ISA is still available to existing customers until 2030, but this difference in limits is undoubtedly confusing. To simplify both schemes and make them fairer for all first-time buyers, the HTB ISA limits should be equalised to the LISA's existing £450,000 cap and then be increased in line with any increases in the LISA limit.

4. **Remove the 12-month rule.** First-time buyers are currently only permitted to withdraw LISA funds after 12 months; any withdrawals before this are considered 'unauthorised' and incur the 25% withdrawal fee. House purchases are complex and cannot always be delayed. Removing this rule would be fairer and make the scheme easier to understand.

Building societies' purpose is to help their customers thrive by promoting resilience through saving. Yet, the LISA's current structure prevents many individuals from benefitting and inevitably results in many losing confidence in lifetime saving or even saving altogether. This would have a detrimental impact on their financial resilience and overall wellbeing[2].

It is our view that retaining the LISA's name and objectives but making some simple yet crucial changes to its rules would make it fairer, easier to understand, and a more attractive option for consumers and financial services providers – three key factors that would increase take-up and allow the LISA to fulfil its intended purpose as a realistic option for lifetime savers.

Questions

Our answers to the below questions incorporate BSA members' individual views and reflect feedback received from the wider sector we represent.

1. Is the Lifetime ISA fit for purpose in its current design, including as a combined product for house purchase and pension saving?

While we are wholly supportive of its intent and the Government's generous 25% bonus, the LISA's rules are overly complicated, its thresholds are no longer viable, and its associated penalties outweigh the benefits.

[1] https://www.ons.gov.uk/economy/inflationandpriceindices/bulletins/housepriceindex/december2023

[2] https://www.bsa.org.uk/getmedia/1c5b562d-84c3-4404-9a21-13bdc1374620/BSA-savings-and-wellbeing-report-FINAL.pdf

Survey results from Leeds Building Society also show that the LISA's complex rules deter customers. Out of 4,000 adults:

- 63% had heard of the Lifetime ISA but half (48%) of these didn't have one
- 27% said they'd avoided it as they didn't understand how it works
- just 12% are currently saving for a deposit are using a Lifetime ISA

Of those not using a Lifetime ISA, the most common reason was that they are already using other savings accounts (36%).

It is inevitable that the complexity of the existing LISA rules deters customers and financial services providers alike; simplifying the product would likely increase availability and uptake.

2. How well do consumers transition between using the Lifetime ISA as a product for house purchase, to then a product for pension saving?
Most of our members do not offer the LISA for the reasons we have already outlined, while for others, the additional operational costs and resource needed to develop the technical aspects[3] of becoming a LISA manager are not yet feasible.

3. Given its policy purposes, is the Lifetime ISA value for money for the Government?
In its current form, the LISA's complexity, usage restrictions, and withdrawal penalties reduce its potential reach and availability across the market – all of which restrict choice, awareness and understanding for consumers. Making the changes we have identified and accompanying its new rollout with simple communications for the public would increase its value for money as more people would be able to take advantage of its benefits.

4. Is the Lifetime ISA a suitable pension savings product?
Not without reform. The LISA's current annual cap of £4,000 significantly reduces its potential as a suitable pension product. Even with a higher annual limit, the LISA's post-tax 25% bonus would still only be suitable for individuals whose earning place them in the 20% tax bracket; others in a higher tax bracket would be better off via the tax relief provided via saving into a pension.

Due to the cost-of-living crisis, the average pension pot needed to meet basic needs in retirement has risen from £70,000 in 2020-21 to nearly £110,000 in 2023-24[4]. With the typical deposit for first-time buyers now around £60,000 across the UK and £144,000 in London[5], it would be impossible within the LISA's current limits for an individual to use the LISA to save for a property and then be able to afford retirement provided for solely by LISA savings.

5. Should the Lifetime ISA be abolished?
No. We are supportive of the LISA's objectives to help first-time buyers take their first step on the property ladder and encourage saving for retirement. It is also our understanding that the LISA technical infrastructure is being leveraged for other

[3] https://www.gov.uk/guidance/apply-to-become-an-approved-lifetime-isa-manager
[4] https://www.livingwage.org.uk/news/pension-pot-needed-basic-retirement-rises-60-cent-nearly-%C2%A3110000
[5] https://www.bsa.org.uk/getmedia/979107ee-ad11-4bb8-ad1c-7e15cf0574fc/BSA-First-Time-Buyers-Report-2024-(Interactive-Single-Page)-(1)_1.pdf

HMRC-led projects, such as ISA digitalisation, so it would not be appropriate to abolish it completely.

However, for the LISA to become a viable long-term savings product, the LISA needs to be simplified, and its rules reformed, to ensure the opportunities it provides reflect the changes in house prices for first-time buyers as well as the economic realities faced by those under cost-of-living pressures.

6. Should the Lifetime ISA be reformed to remove the withdrawal penalty?
The current 25% withdrawal penalty results in many people losing a proportion of their own hard-earned savings in addition to the Government bonus (*example below) if they withdraw their funds outside of the existing LISA rules. Even if somebody uses the LISA to purchase their first home, which was its intended purpose, they would still be penalised and lose some of their own money if they purchase a property priced above the threshold. This policy is draconian, complex, and fundamentally unfair. According to HMRC LISA data from the 2023-2024 tax year, there were 42,750 more individuals making unauthorised LISA withdrawals than individuals withdrawing their LISA funds for a permitted house purchase. This is not surprising given the limits currently in place have not been raised since the LISA was introduced in 2017. However, it shows a major disconnect between the LISA scheme and its beneficiaries. It is also one of the main reasons that prevents many of our members from offering the LISA.

We believe a deterrent is appropriate to discourage savers from withdrawing their funds early and ensuring the spirit of the LISA remains intact; however, any charge applied must be fair. Many people are also still struggling with cost-of-living pressures and should be permitted access to their own money in times of need. We therefore feel it would be appropriate for anybody needing to withdraw their savings early to forfeit the Government bonus, but they should not risk ending up with less than they initially invested.

A reduction in the withdrawal charge from 25% to 20% would ensure the spirit of a long-term savings scheme remains intact, without deterring young savers from registering in the first place in case they need to access their savings early. This change was introduced on a temporary basis during the COVID-19 pandemic (6 March 2020 – 5 April 2021) and provided much needed support to consumers in difficult times. We have heard from an existing LISA provider that savers continued to be highly motivated to save for a property purchase even when the withdrawal fee was temporarily reduced; losing the Government bonus was a strong incentive for the saver to keep their savings in their LISA if they were able to but they could rely on the stability of knowing they could withdraw their funds if needed.

We believe this change should be re-introduced on a permanent basis. We should not penalise savers for trying to keep to the original intent of the scheme, particularly with the current cost-of-living challenges that mean they may need to access their savings.

If unauthorised withdrawals had been penalised at 20% since the LISA was introduced, the Exchequer would have foregone just £35.6 million (assuming the same number of withdrawals). This seems a small price to pay for the harm done to the image of the LISA product and the unfairness felt by those savers penalised because they were caught out by rising house prices.

***Example**
For somebody who has saved £4,000 per year for five years in a LISA, the penalty for using their savings towards buying a house above the £450,000 threshold would be the entire government bonus plus an extra £1,250 of their own savings.

7. Should the Lifetime ISA be restricted to those with no access to a workplace pension?
No, it should not be restricted. For those in the 20% tax bracket, the LISA has the potential to offer greater benefits than the tax relief provided by a workplace pension. More choice also encourages competition in the market and ultimately benefits consumers. However, communication needs to be clearer and additional published guidance would be beneficial to ensure people are able to make their own well-informed financial decisions.

8. Should the Lifetime ISA house price cap be raised in line with inflation, or removed?
We do not believe the house price cap should be removed completely – we understand that appropriate guardrails are reasonable to ensure the incentive is well targeted to those who need it most. However, the £450,000 house price cap should be increased in line with house prices, which have risen by at least 30% since the LISA was introduced in 2017. This threshold is too restrictive in certain parts of the UK and is preventing many first-time buyers from buying their first home. It is our view that the limit should be increased to £585,000 and then reviewed on an annual basis.

The HTB ISA thresholds should also be amended – the HTB ISA's current structure with two different thresholds is unfair and adds unnecessary complexity to a very similar product to LISA. It is our view that this should be increased and brought in line with LISA so there is only one limit of £585,000. This should also be reviewed annually in the same way. If this is not possible for any reason, the Government should consider allowing full transfers from the HTB ISA to a LISA.

For shared ownership properties being purchased using LISA funds, the cap should reflect the value of the percentage being purchased rather than the total value of the property.

9. Should the annual Lifetime ISA limit be raised from £4,000?
Yes. Although we do agree that an annual limit is appropriate to help spread the benefits of the Government bonus to a greater number of people, the current annual limit of £4,000 is too restrictive.

Currently, the LISA can only be opened by individuals aged between 18 and 39 and they can only save into a LISA until the age of 50. This gives them 32 years to save for a house deposit and retirement. Given the average deposit for first-time buyers is between £60,000 and £144,000, and the average pension pot needed to meet basic needs in retirement nearly £110,000, it would be impossible within the LISA's current limits for an individual to use the LISA to save for a property and retirement using solely their LISA funds – even with the bonus.

To ensure the LISA can feasibly be used for both its intended purposes, we recommend raising the maximum age for opening a LISA to 50 and allowing deposits into the LISA until the age of 60.

10. Should the Lifetime ISA be reformed in any other way?
Our members hold nearly half the UK's cash ISA balances, but only a select few offer the LISA in its current form. This is primarily due to its complexity, its punitive rules, and the current lack of consumer awareness of the LISA compared to other ISA types.
To boost uptake and consumer understanding, the Government should consider simplifying the LISA and making it fairer by:

- lowering the withdrawal penalty to 20%. This would prevent people from benefitting from the Government bonus if they are using the LISA improperly but without losing their hard-earned savings if they need access to their funds.

- increasing the property price cap to £585,000 in line with the rise in house prices and reviewing this on an ongoing basis

- increasing and aligning the HTB threshold with the LISA threshold and reviewing it on an ongoing basis OR permitting full transfers from HTB ISAs to LISAs without impacting the individual's limits

- amending the property price cap for shared ownership properties to reflect the contribution value rather than the total value of the property

- raising the maximum ages to open and save into a LISA to 50 and 60 respectively, to ensure it can be used for both purchasing a property and as a feasible retirement fund

- updating communications and publishing additional guidance to increase public awareness of the LISA's benefit and limitations.

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