Consumer risks associated with proposed changes to the Cash ISA regime

The negative customer impact of a reduction in the Cash ISA allowance.

newcastle.co.uk

Newcastle Building Society

Executive summary

The Cash ISA is a savings success story. Recent HMRC data shows that Cash ISAs continue to be a popular choice for savers, holding c£297bn of balances. All whilst remaining easily accessible to ordinary people in the UK – often those building healthy savings habits over long periods and looking to make the most of their modest savings pot.

The Building Societies Association (BSA) continues to make a compelling argument against limiting consumer choice by reducing Cash ISA limits, especially given the important role that Cash ISA balances play in underpinning the UK mortgage market. We agree with the arguments stated by the BSA, the purpose of this report is to shift focus onto the customers who stand to be most impacted by proposed changes to the Cash ISA allowances.

As the BSA has done, it's important to state that we wholeheartedly support the Government's intent to boost UK investment. But this won't be achieved by reducing the Cash ISA limit because it presupposes that Cash ISA customers can and should want to move their tax-free savings to higher risk, longer term options, including much more complex instruments and asset classes.

The reality of the Cash ISA customer is that they are invariably modest savers, from low-to-middle income households, relying on traditional savings as they build to, or manage in, retirement. For many of these people, a Stocks and Shares ISA would not be an appropriate savings vehicle and it would be wrong to push them in that direction.

It is our view that restricting Cash ISAs in the hope that savers will be enticed towards equity-based investments which may not be suited to their needs, investment horizon, nor their risk appetite, could have serious negative consequences for many of our customers.

Getting to know the real Cash ISA savers

Cash ISA savers, some of whom have families, some who live alone, are people who have likely spent years planning and striving to secure a steady financial future.

There is a misguided assumption that those who will be most affected by the proposed changes to the Cash ISA limits are a universally financially sophisticated group, who could just as easily and comfortably invest in the stock market as save in a Cash ISA.

In our experience, this is not the case and the make-up of our Cash ISA customer base challenges this presumption:

- Our ISA customers are predominantly older or approaching retirement. 67% of them are aged 60+, and over 50% of them are beyond the state retirement age.
- Within the 60+ age group, 45% are likely to be living in down-sized accommodation, using traditional methods to manage their finances. Some will have built up savings and investments, although perhaps to a lower value than average.
- Our Cash ISA customers within the 45-54 age range are typically working families - often couples with older children - their savings and investments tend to be moderate with nearly a quarter putting money aside on a regular basis.
- They typically have a lower appetite for risk and a more limited capacity for loss due to the stage they are in life.

Far from ISA millionaires, our Cash ISA savers have relatively modest holdings to support their retirement living, or their plans toward retirement.

Almost 95% of our ISA customers aged over 60 hold balances under £100k, often managing on a budget. They have placed their trust in accessible tax efficient savings as a key source of financial security in later years.

Cash ISA customer, Brian Stobbs

Brian Stobbs, 61, has lived in Consett, County Durham, his entire life and is the former head of asset management for the Durham Aged Mineworkers Homes Association.

> *I've been a loyal Cash ISA saver since the 1990s, and am proud to say that in more recent years I've been able to make full use of my tax-free limit. My ISA provides the access and freedom myself and my wife Kathryn want to be able to enjoy our retirement on our terms.*
>
> *I'm not keen on risk and I don't want to be forced into a Stocks and Shares ISA where my money could be gambled on the markets, or feel like I'm bank-rolling the economy. Forcing me into a risky product undermines everything a Cash ISA stands for.*

The regressive impact of proposed Cash ISA reforms

As outlined above, it would not be appropriate for many Cash ISA customers to move their savings to higher risk, longer term, and less liquid investments. Very few of our Cash ISA customers are likely to save to the annual ISA limit every year, and unlike pensions, ISA allowances are lost once the end of the tax year has passed. Many accumulate their ISA savings over time and rely on the current limit for strategic financial planning – such as using their ISA allowance over several years following windfall events (e.g. inheritance, redundancy, or property downsizing).

Altering the allowance risks alienating these groups and may discourage saving altogether, particularly among lower-income households.

Cash ISAs appeal to savers who have low levels of financial resilience/income.

Research shows that 65% of Cash ISA customers who have a household income less than £15.5k have deposited into an ISA in the last 12 months (Mintel Research – ISA Report September 2024).

The current limit encourages low risk, healthy savings habits, building financial resilience and self-sufficiency. People who rely on their Cash ISA allowance as a source of financial security are also often the same people who prefer to open and manage their ISAs in person – typically older generations who are uncomfortable with online banking or prefer to trust their local branch.

Reducing the benefits of these products will further accelerate the trend of customers disengaging with high-street banks and building societies and possibly with saving more widely.

Further market insight

- The average Cash ISA subscription held across the market stands at £15.3k (Newcastle Building Society's average is higher at £18.3k), illustrating the value people place on the product. (CACI Data Stock position end of December 2024).
- Many savers prefer products that provide guaranteed returns, with 62% of people surveyed showing a preference for a savings account, and with 34% showing preference for a Cash ISA. Only 14% of those interviewed said they'd choose a Stocks and Share ISA. Mintel Research – ISA Report September 2024.
- Lack of understanding of ISAs is impacting the potential size/opportunity of the ISA market. Mintel's research shows that 68% of savers have not invested into an ISA. Mintel Research – ISA Report September 2024.

- The Cash ISA market has increased in size over the last couple of years (c.£97bn since Jan 2023), as market volatility has seen investors move money out of Stocks and Shares ISA into Cash ISAs. (Bank of England data).
- The average 1 year fixed rate ISA rate across the market in 2024 stood at 4.46% (Newcastle Building Society paid on average 4.5%), evidencing healthy returns available. (Bank of England & CACI data as at end of December 2024).

Existing transfer flexibility makes structural change unnecessary

Under current rules, consumers already have the freedom to transfer funds from a Cash ISA to a Stocks and Shares ISA without losing tax advantages.

- This means the system already allows savers to rebalance between safety (cash) and growth (investment) as their financial goals evolve.
- Rather than altering limits or forcing choices, we'd argue that policy should focus on better articulating and promoting this flexibility, empowering individuals to make informed decisions.
- Default to cash is a consequence of the financial information and advice gap.

There are already reforms underway designed to close that gap - in particular the Financial Advice Boundary Review. If these are successful they will encourage more people to consider Stocks and Shares ISAs – particularly those younger or mid-life savers with longer horizons.

Such reforms should be given time to impact behavioural change driven by appropriate advice, rather than using the blunt instrument of restricting choice.

Conclusion

Reducing the Cash ISA allowance would undermine the broader goals of expanding financial inclusion and choice.

For the modest Cash ISA saver – typically older, from a lower-to-middle income background – it would be inappropriate to seek higher-risk, longer term investments. Indeed, the reason the Cash ISA continues to be a success is its accessibility as part of a healthy savings culture.

It's vital that those shaping policy making consider the reality of the Cash ISA saver and how changes could risk the financial security of UK savers up and down the country.

For further information contact:

Kathryn McLaughlin, Head of Group Corporate Affairs
kathryn.mclaughlin@newcastle.co.uk
07575 474 741

Principal Office: 1 Cobalt Park Way, Wallsend, NE28 9EJ
newcastle.co.uk

Newcastle
Building Society

Principal Office: 1 Cobalt Park Way, Wallsend, NE28 9EJ
newcastle.co.uk