



AJ Bell Policy Paper

The case for radical ISA simplification

Foreword by Michael Summersgill

Why does AJ Bell keep banging on about simplification of the financial services landscape for retail investors? The UK capital markets face well documented challenges, yet we have not created an environment that ensures we get the highest possible participation in our own capital markets from our own citizens. There are many improvements that could be made, but addressing complexity seems to me to be the bare minimum any government serious about encouraging greater levels of long-term investing should aim for.

There is now a mountain of behavioural economics research which tells us too much choice can lead to people feeling overwhelmed, resulting in low levels of engagement. AJ Bell's consumer research, detailed in this report, supports this contention.

It is at this point the financial services industry often takes a wrong turn. "We should put Finance on the National Curriculum", "We need to teach this stuff in schools". Financial literacy education was added to the National Curriculum in September 2014. It didn't work. Research proves that the elapsed time between the 'intervention' and the decision point renders such education largely ineffective in helping citizens to navigate the complexities of the financial services landscape they encounter throughout their adult lives.

This is why simplicity is key. Given many people already perceive long-term investing as too difficult, it is vital we attempt to drive greater engagement by ensuring the investment landscape people encounter is as straightforward as possible to navigate.

Which brings me to ISAs, one of those rare things in financial services – a product created by government that has been a roaring success. The ISA success story has been delivered in part because of the flexibility and tax efficiency of the product, but also because it has been, until recently, simple to understand.

Mounting complexity risks undermining that success. From straightforward beginnings, there are now six different versions of ISAs available to UK investors, with different rules and limits confusing people. A seventh ISA type, the ill-conceived 'UK ISA', was proposed by the previous government but has not yet been introduced. We hope it isn't.

With policymakers focused on boosting long-term investing and getting more capital flowing to UK businesses, now is the time to bring forward radical ISA simplification, possibly starting by merging Cash and Stocks and Shares ISAs, but with the ultimate goal of moving to a single 'One ISA' regime. Removing the upfront complexity millions of investors face, combined with efforts to improve the quality of financial guidance and promote the benefits of regulated advice, would provide a more sensible foundation to build a genuine long-term investing culture in the UK.

From this basis, further reforms aimed at encouraging money to flow to UK business can be considered. Given around half of assets held on AJ Bell's platform are UK-focused, simply increasing the overall ISA allowance from £20,000 to £25,000 should naturally drive more money towards UK plc. Creating a genuine incentive to invest in UK assets, such as by scrapping stamp duty on UK investments, would also help achieve this aim. Or even more radical, the inheritance tax exemption enjoyed by AIM stocks could be extended to include UK listed shares and those funds that invest in them.

A new government with a fresh mandate has the opportunity to seize the agenda by delivering fundamental reforms that will encourage long-term investing. If Labour can grasp the nettle by radically simplifying ISAs, it can establish a foundation upon which the future prosperity of savers and ultimately UK businesses can be built.



Executive summary

ISAs have been one of the UK's success stories in helping people save and build resilience into their financial well-being.

By offering a simple route to investing and meaningful tax advantages, coupled with flexibility on both subscribing and withdrawing money, ISAs have been instrumental in encouraging a culture of long-term saving and investment in the UK.

The ISA brand is strong. Nearly £750bn is held in ISAs owned by UK adults. That includes around £456bn invested in Stocks and Shares ISAs and £285bn in Cash ISAs. A further £9bn is held in Junior ISAs for children.

However, this success risks being undermined by mounting complexity. There are now six different versions of ISAs with different rules, benefits and limitations which can be confusing for consumers. AJ Bell research¹ found half (49%) of UK adults think the different versions of ISAs make them too complicated.

The way forward

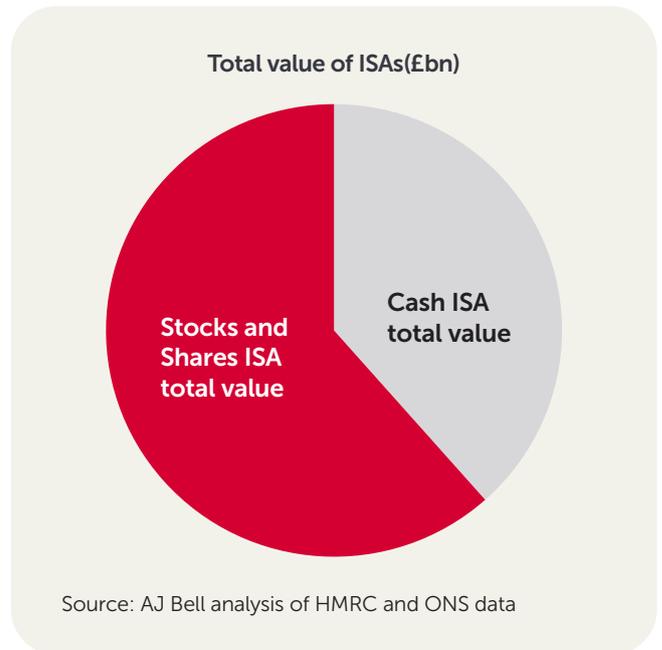
The new government has an opportunity to stamp its mark on UK saving and investing; to constructively help UK savers and investors build financial resilience and enable people to enjoy a more prosperous life in the future.

We need to make sure ISAs are fit for purpose by radically simplifying the number of ISA types, so people feel more assured just making the decision to save, without the option of 'into what?', leading to procrastination or abandoning the intention altogether.

This coupled with a new and strong Targeted Support environment (as discussed in the joint FCA and Treasury consultation²) to help individuals navigate investment choices and make informed decisions, will directly build financial resilience as well as boost investment in UK businesses, enabling them to grow and expand.

AJ Bell recommends the government should:

1. **Radically simplify the ISA regime** – combine the Cash, Stocks and Shares, Junior and Innovative Finance ISAs into a single ISA product with a higher allowance of £25,000. Individual administrators would have the flexibility to choose which investments to allow within this simplified ISA.
2. **Launch a Targeted Support regime and promote the value of regulated advice** – to help investors make informed decisions, government and regulators should proceed with proposals to introduce Targeted Support and conduct further work to promote the value of regulated financial advice.
3. **Ditch the planned UK ISA and abolish stamp duty on UK shares** – the UK ISA proposed by the previous government, while well-intentioned, was always doomed to fail in its objective of boosting UK capital markets and stimulating economic growth. Scrapping stamp duty on UK shares would create a genuine incentive for investors to support the UK stock market.



¹ AJ Bell Research (2023) carried out in March 2023 by Opinium. Nationally representative sample of 2000 UK adults. Full results in Appendix 1.

² DP23/5 Advice Guidance Boundary Review – proposals for closing the advice gap (December 2023)

Complexity risks undermining the ISA success story

Lack of understanding is one of the biggest barriers to investing. AJ Bell's core purpose is to help people invest. We do that by making investing as easy as possible, but our customers often come up against unnecessary complexity in the rules governing financial products.

ISAs are a classic example of this. From simple beginnings 25 years ago, interventions by successive governments mean there are now six different versions of ISAs. The current ISA landscape is:

- Stocks and Shares ISA
- Cash ISA
- Junior ISA
- Lifetime ISA
- Help to Buy ISA (now closed)
- Innovative Finance ISA

The Conservative government even proposed a seventh ISA – the UK ISA – going as far as launching a consultation, which closed in early June, on the detail.

Unsurprisingly, ordinary people struggle to get to grips with this complexity. AJ Bell research³ shows, despite 71% of UK adults saying they are familiar with ISAs, fewer than a third (29%) know the current adult ISA allowance is £20,000. This falls further for women to 26% and further still for young adults aged 18-34 (19%).

Furthermore, half (49%) of UK adults think the different versions of ISAs make them too complicated. Although Cash ISAs had some recognition, fewer than half of UK adults could recognise the other types.

Financial advisers have similar concerns, with AJ Bell⁴ research showing the vast majority of financial advisers support ISA simplification. Two-thirds (65%) believed unnecessary complexity had crept into the ISA market, and 8 in 10 (77%) thought this was down to 'too many variants and names' for ISA products.

To put it simply: ISA complexity risks putting people off saving and investing for the long-term. Without radical simplification, there is a danger ISAs will not achieve their full potential, reducing their appeal to savers and undermining efforts to boost long-term investing, including in the UK.

Recent ISA changes did not go far enough

The previous government's ISA interventions demonstrated little by way of a long-term vision. In the 2023 Autumn Statement, the Treasury appeared to be moving in the direction of ISA simplification, although the changes announced – the most significant of which was allowing people to subscribe to multiple versions of the same ISA in a tax year – were relatively unambitious.

However, months later, chancellor Jeremy Hunt used his March Budget to unveil plans for a new type of ISA – the UK ISA – aimed at encouraging UK savers to invest more in UK companies. Creating a new type of ISA would clearly have run counter to the previously stated goal of simplification and is emblematic of the lack of strategic thinking from policymakers. ISA reform should focus on making it easier for people to take the first step and invest for the long-term, which will naturally benefit UK companies and the UK stock market.

Labour's commitment to simplifying ISAs

Labour is taking a different stance.

In its paper *Financing Growth: Labour's Plan for Financial Services*, Labour committed to looking to simplify the ISA landscape to make it as easy as possible for people to feel the benefits of saving and investing their money, including through increased utilisation of Stocks and Shares ISAs.

³ AJ Bell research carried out in March 2023 by Opinium. Nationally representative sample of 2000 UK adults. Full results in Appendix 1.

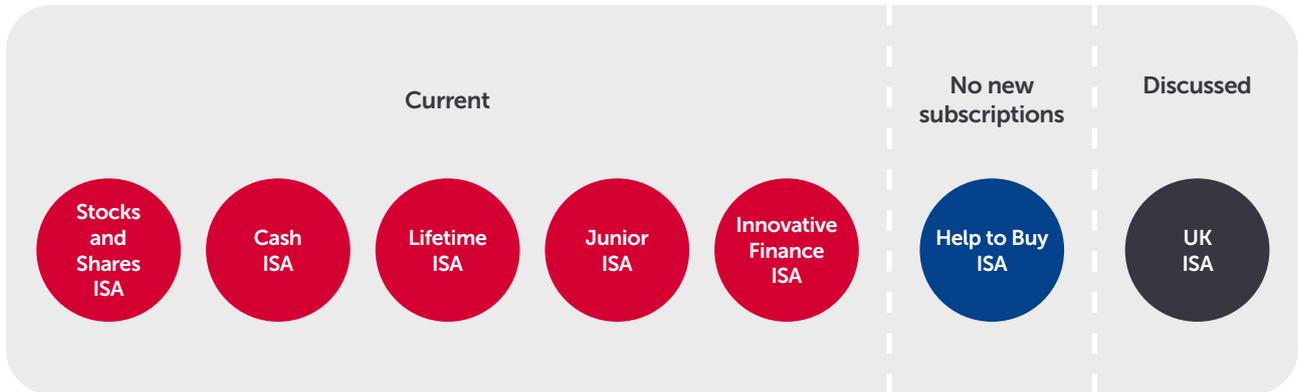
⁴ AJ Bell research carried out in August 2023 with 349 financial advisers. Full results in Appendix 3.

Benefits of ISA simplification

The reasons AJ Bell started campaigning for ISA simplification several years ago are still as relevant now as they were then.

As a nation, we need to widen accessibility and encourage greater participation in long-term saving and investing, helping people in the UK build financial resilience today and save for later life. UK investors also need to be encouraged to move from the 'safe harbour' of cash – which will be eaten away by inflation – into long-term investing. ISAs are the perfect vehicle to do this. Notwithstanding the complexity introduced over the years, the ISA brand is well-known and trusted and one which the government should put at the heart of its policy around savings and investments.

The wide variety of ISAs available offers a degree of flexibility, but as our research proves, it can also confuse consumers, leading to 'analysis paralysis' and deterring people from taking that first step to open an account and start investing.



Radical simplification can make ISAs more accessible to a broader range of individuals, including those with lower financial literacy. By streamlining the options and reducing jargon, the upfront choice new investors face can be stripped back, removing a key barrier to investing through ISAs. When individuals feel more empowered to make informed decisions about their finances, they are more likely to commit to regulator contributions and investment strategies. This, in turn, will naturally benefit UK capital markets.

This is backed up by our research⁵: 48% of UK adults agree a single ISA would make them easier to understand and almost a third (30%) said they'd save more in ISAs if they were less complicated.

And 78% of financial advisers⁶ agree too many variants and names has led to unnecessary complexity creeping into the ISA market.

⁵ AJ Bell research carried out in March 2023 by Opinium. Nationally representative sample of 2000 UK adults. Full results in Appendix 1.

⁶ AJ Bell research carried out in August 2023 with 349 financial advisers. Full results in Appendix 3.

AJ Bell's One ISA proposal

Our ISA policy paper⁷, published last year, proposing a single 'One ISA', combining the best features of the current regime with the simplicity of consolidating the six ISAs into a single ISA product, was positively received by government and the industry.

Most agreed with the main thrust of our call for radical simplification and recognised a single product could help encourage more people to invest outside of cash, diversifying their savings and enabling people to realise their long-term goals. However, we accept the Lifetime ISA, which has a bonus element linked to how the funds are eventually used, complicates matters both practically and politically.

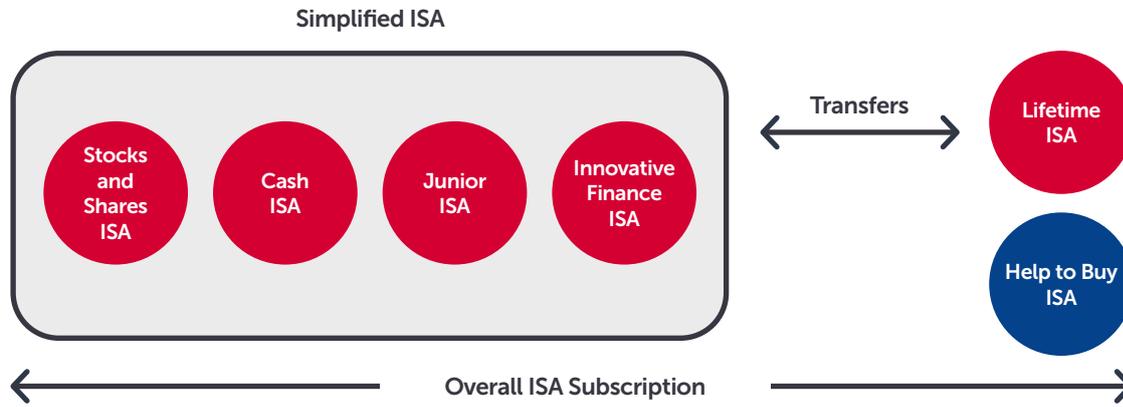
After reflecting on our original proposals, we are still committed to creating a single ISA combining the six different versions into one over the long-term. However, recognising the challenges associated with the Lifetime ISA, as a first step we recommend the government combines the following ISA types into a single ISA:

- Cash ISA
- Stocks and Shares ISA
- Junior ISA; and
- Innovative Finance ISA

The Lifetime ISA and Help-to-Buy ISA would remain outside the simplified ISA framework for now but continue to interact with the ISA as they do today. Transfers could be made, as now, between Lifetime ISAs and the simplified ISA. An overall, higher, £25,000 ISA subscription limit (see below) would be applied to subscriptions made to both the ISA and the Lifetime ISA. The Lifetime ISA would retain its separate payment limit (which includes any subscriptions made to a Help-to-Buy ISA).

Proposed simplified ISA structure		
Annual ISA allowance	Under 18	£9,000, rising with CPI each year
	18 or over	£25,000 or in-force ISA allowance at introduction if higher, rising with CPI each tax year
Eligibility	UK resident Person with parental responsibility will be responsible for ISA for under 16s	
Permitted investments	As for current stocks and shares ISA	
Tax treatments	No capital gains tax on realised gains or income tax on interest or dividends	
Withdrawals	Allowed from age 18 onwards, with no withdrawal penalty	
Transfers	Full and partial transfers allowed	

Importantly, under our proposal providers would be able to choose which investments to allow within the main ISA structure. For example, a building society currently offering a Cash ISA could offer exactly the same investments under the reformed ISA. Equally, a platform offering a Stocks and Shares ISA could continue to offer these investments. But rather than the ISA being defined by how people can invest, the investment options would simply be a feature of each ISA determined by the ISA provider, just as investments are a feature of pensions. After all, we don't have a Cash pension, a Stocks and Shares pension nor a Lifetime pension.



Creating a simplified ISA means people do not need to make the initial decision of where to save – in a Cash ISA or a Stocks and Shares ISA. Instead, they just save in an ISA. It makes it easier for those who are ready to take the next step in their savings journey – they can move from cash to investment easily within a single tax wrapper (provided the firm offers both cash and equity investing options). This fluidity will make it simpler for ISA managers and others to encourage more diverse investment for many consumers.

Increasing the overall ISA subscription to £25,000

In March 2024, the Treasury launched a consultation on how to implement a UK ISA.

This was an ill-conceived political gimmick, which would have added a seventh ISA type creating even more complexity. There is a real danger this would have led, over the long-term, to fewer people investing through ISAs.

Given about half of AJ Bell ISA customers' assets are already invested in UK companies and funds, if the government wishes to prioritise investment in UK businesses, then increasing the ISA allowance to £25,000 will naturally increase investment in UK plc.

Improving the Lifetime ISA

The terms for the Lifetime ISA have not changed since being introduced seven years ago and need updating to be financially fit for the mid-2020s.

If the subscription level of £4,000 had been increased each year in line with CPI inflation it would now be set at £5,148.⁸ If it had been linked to house inflation for the same period, it would have increased by 24.2%.⁹ We recommend it is increased to £5,000.

The first house property limit was set at £450,000 in April 2017 and has not been reviewed for seven years. If the property limit had risen with house price inflation, then it would now be worth £558,194. However, it could be aligned with the first-time buyer stamp duty threshold of £625,000.

The 25% early withdrawal charge – which effectively acts as a 6.25% penalty – also complicates the product. We recommend the government cut this charge from 25% to 20%, meaning it only returns the upfront bonus, with no additional penalty. This adjustment was made during the pandemic to ensure those accessing their Lifetime ISA whilst facing serious hardship were not unfairly penalised. To simplify the product, the withdrawal charge should be reduced to 20% permanently.

Setting a penal 6.25% exit charge is at odds with the transparent modern ISA product operating within the Consumer Duty environment. In its guidance on the Consumer Duty released in 2022¹⁰, the FCA said firms should not charge 'unreasonable exit fees that discourage customers from leaving products or services that are not right for them'.

Recommended terms for the Lifetime ISA:

- Increase the subscription level, say to £5,000
- Increase the price limit for first house purchase, say to £625,000
- Reduce withdrawal charge to 20%, only pay back the bonus and not an additional withdrawal penalty of 6.25%

⁸ Bank of England inflation calculator – over the period 2017 to March 2024

⁹ Nationwide House Price index. A UK average house valued at £450,000 in Q2 2017 would be worth £558,194 in Q1 2024.

¹⁰ FG22/5: Final non-Handbook Guidance for firms on the Consumer Duty

Appendix 1: AJ Bell research: Consumer understanding of ISAs (March 2023)

Q1: To what extent are you familiar with ISAs (Individual savings accounts)?

Answer	Number of responses	Percentage	Net Percentages
I am familiar with ISAs and have money in them	812	40.6%	71.2% (familiar with ISAs)
I am familiar with ISAs, but do not have money in them	612	30.6%	
I have definitely heard of ISAs before today	411	20.5%	96.5% (aware of ISAs)
I think I have heard of ISAs before today	95	4.8%	
I have never heard of ISAs before today	70	3.5%	3.5% (completely unaware of ISAs)

Source: AJ Bell, Opinium. Survey of 2,000 people conducted between 14-17 March 2023.

Q2: Which, if any, of the following do you think are type(s) of ISAs (Individual savings accounts)? Please select all that apply.

Answer	Number of responses	Percentage
Cash ISA	1262	63.1%
Stocks and shares ISA	886	44.3%
Junior ISA	755	37.8%
Lifetime ISA	721	36.0%
Help to buy ISA	641	32.0%
Flexible ISA	437	21.9%
Innovative finance ISA	148	7.4%

Source: AJ Bell, Opinium. Survey of 2,000 people conducted between 14-17 March 2023.

Q3: Which of the following do you think is the maximum amount you can save into ISAs each year?

Answer	Number of responses			Percentage		
	Male	Female	Total	Male	Female	Total
£20,000	312	269	582	32.1%	26.5%	29.1%

Source: AJ Bell, Opinium. Survey of 2,000 people conducted between 14-17 March 2023. Totals may be higher than combined Male and Female totals due to additional gender options of 'Prefer not to say' and 'Other'.

Q3: Which of the following do you think is the maximum amount you can save into ISAs each year?

Answer	Number of responses			Percentage		
	Age 18-34	Age 35-54	Age 55+	Age 18-34	Age 35-54	Age 55+
£20,000	108	199	275	19.3%	30.3%	35.1%

Source: AJ Bell, Opinium. Survey of 2,000 people conducted between 14-17 March 2023.

Q4: Which of the following do you think is the maximum you can personally save into a Lifetime ISA (up until the age of 50) each year – not including the Government bonus?

Answer	Number of responses				Percentage			
	Age 18-34	Age 35-54	Age 55+	Total	Age 18-34	Age 35-54	Age 55+	Total
£4,000	82	44	22	148	14.5%	6.7%	2.8%	7.4%

Source: AJ Bell, Opinium. Survey of 2,000 people conducted between 14-17 March 2023.

Q5: What level of tax do you think you pay on the following?

Answer	Income tax paid on interest and dividends within an ISA		Capital gains tax paid on investment gains within an ISA	
	Total	Percentage	Total	Percentage
0%	677	33.8%	530	26.5%
10%	116	5.8%	109	5.5%
20%	197	9.9%	174	8.7%
30%	61	3.0%	65	3.3%
40%	37	1.8%	61	3.1%
45%	12	0.6%	19	0.9%
More than 45%	7	0.3%	3	0.1%
Depends which income tax band you are in	138	6.9%	158	7.9%
Not sure/don't know	755	37.8%	881	44.0%

Source: AJ Bell, Opinium. Survey of 2,000 people conducted between 14-17 March 2023.

Q6: To what extent do you agree or disagree with the following statements?

Answer	The different versions of ISAs make them too complicated		A single ISA product, rather than multiple products, would make them easier to understand		If ISAs were less complicated, I'd save more in them	
	Total	Percentage	Total	Percentage	Total	Percentage
Strongly agree	295	14.8%	301	15.0%	162	8.1%
Agree	688	34.4%	657	32.9%	433	21.6%
Neither agree nor disagree	462	23.1%	516	25.8%	598	29.9%
Disagree	214	10.7%	128	6.4%	345	17.2%
Strongly Disagree	87	4.3%	45	2.3%	185	9.2%
Not sure/don't know	254	12.7%	352	17.6%	278	13.9%

Source: AJ Bell, Opinium. Survey of 2,000 people conducted between 14-17 March 2023.

Appendix 2: AJ Bell Research: Consumers and the UK ISA (May 2024)

Question 1: Finances of UK adults:

- 42% have cash savings of £10,000 or more.
 - 52% of those age 55 and above
 - 38% of 35 to 55-year-olds
 - 33% of 18 to 34-year-olds
- 35% have cash savings of under £10,000
- 20% don't have savings.

Question 2: Choice of ISA when investing for the first time in a tax year

Products UK adults would use if they were investing into an ISA to invest for the first time in a tax year

UK ISA	35%
Stocks and Shares ISA	26%
Don't know	43%
Other	3%

Research carried out by Opinium between 7 May 2024 and 10 May 2024. Sample of 2,000 UK adults.

Appendix 3: AJ Bell Research (August 2023) – Financial advisers' view of ISA regime

Question 1: Do you think unnecessary complexity has crept into the ISA Market?

Yes	65.9%
No	34.1%

Question 2: If yes, what do you think has caused this complexity? Tick all that apply

Too many variants and names	77.5%
Restrictions over only being allowed one type of ISA a tax year	34.6%
The Lifetime ISA rules	42.5%
How ISA funds are passed to spouses on death via an additional permitted subscription	26.3%
Other	4.2%

Question 3: Do you support the concept of having one ISA product that covers all the existing benefits of ISAs?

Yes	84.0%
No	16.0%

Question 4: Are there any enhancements that would make ISAs more valuable to your clients? Tick all that apply.

Expanding the age limit for Lifetime ISAs as a retirement savings vehicle	35.8%
Allowing ISA flexibility to span more than one year	45.8%
Expanding the ISA-eligible investment universe	14.6%
Allowing CGT-free disposals to fund ISA top ups	46.4%
A carry forward element to the ISA subscription limit	74.5%
Other	7.7%

Research carried out by AJ Bell with 349 financial advisers in August 2023.

