Saving for a sustainable future

Increasing public benefit from UK tax relief for savings

by Chris Hewett

green alliance...

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Green Alliance
Green Alliance is a charity and independent think tank focused on ambitious leadership for the environment. We have a track record of over 30 years, working with the most influential leaders from the NGO and business communities. Our work generates new thinking and dialogue, and has increased political action and support for environmental solutions in the UK.

This pamphlet is produced as part of Green Alliance's Sustainable Economy theme which looks at how to use the big economic levers of private investment, taxation, and public spending to accelerate the low carbon economic transition.

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A broken savings and investment cycle

Savings and investment is a cycle as old as capitalism itself. People save to increase their personal financial security and the capital is reinvested in the economy so business can grow, infrastructure can be built and innovations created. But in the UK this cycle has broken. We are at the bottom of the OECD league for the amount we save as families and invest as an economy. Public trust in the financial services sector has fallen dramatically, and many economists are concerned about the growing culture of short termism that permeates the investment community. Meanwhile the challenge of climate change means we need economic recovery to involve higher levels of investment than ever before to deliver a low carbon transition.

Three building blocks for sustainable, investment led, recovery

This report proposes a new policy agenda to restore the savings and investment cycle as an engine for economic stability, social innovation and low carbon economic transition. The foundation of this new agenda needs three important building blocks.

First, public trust must be restored in financial institutions to the degree that the savings culture is revived in UK society. A higher rate of savings would help us to adjust to the challenge of an ageing population, increase the pool of capital available for investment and reduce over-dependence on consumer spending for prosperity.

Second, we need to find ways to give greater reward to long term investment, which would reverse the trend of short termism that has undermined productive sectors of the economy and provide a greater stability for business and innovation.

Finally, we need a higher proportion of the increased savings and investments to flow towards the vast range of activities that will increase our energy security, reduce carbon emissions and enhance social and environmental well-being, as well as provide financial returns.

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Encouraging sustainable savings and investment

The government already has a number of policies designed to encourage saving and investment. It gives up to £40 billion per year in tax relief for ISAs, pension contributions, venture capital and property investment, yet there is nothing attached to these subsidies to encourage responsible or sustainable investment.

It is our belief that policy makers, the public and the financial services industry need to consider and debate seriously a new principle that, in return for tax relief and implicit subsidy, savers and investors should be able to demonstrate a contribution to the public good.

This would manifest itself in some fundamental changes over the next few years:

- Favourable tax treatment of pension contributions and private equity investments, such as Venture Capital Trusts, should be reformed in ways that require proof of responsible investment and asset management that genuinely reflects the long term interests of pension holders, and taxpayers.
- Banks and building societies would only be eligible to offer tax free ISA savings accounts if they can prove responsible lending practices, including far greater transparency of the types of economic activities supported by their lending.
- The exemption of residential property from capital gains tax could depend on proven energy efficiency improvements made to the fabric of the building during the period of ownership.

Such changes could not be carried out quickly, but the government could explore the feasibility of putting these principles into action by introducing some interim measures to test the reactions of the savings and investment market. For example:

- Grant an extra £3,000 ISA allowance for individuals to save in green or social stocks and shares ISAs, including the extension of the ISA eligibility to include corporate green bonds.
- Increase the investment limit for Venture Capital Trusts and Enterprise Investment Scheme funds which invest in clean technology or social enterprise.

1. Introduction

Saving and investment is a cycle as old as capitalism itself. It is the foundation of the banking system and the way that money generated from income and profits is recycled through the economy so that businesses can grow, infrastructure can be built and innovations created. This cycle has great public and private benefits. A family that is able to save has greater resilience to economic shocks. An economy that has high levels of capital being invested has good future prospects. But the UK has a poor record on both saving and investment levels which has contributed to current difficulties. Rebalancing the economy after the financial crisis will require a more active policy to rejuvenate this cycle.

Why do we save?

Most people earn income for a limited period in their lives. During that period, if their income is high enough, they put some aside for periods when they either want to spend a large sum of money, on a house, a car, a holiday, or for when they know their income will decline, when they are older or during periods of unemployment. Those savings will be deposited in financial institutions (banks, building societies, pension funds), and form part of the capital that is then reinvested in the economy to buy homes, grow businesses, build infrastructure and create wealth for future generations. For some the purchase of property itself has become a form of saving for the future, either to generate income through renting, or as a capital asset that can be sold later in life.

In the years before the credit crunch the UK suffered from over borrowing and under saving, certainly at a consumer level and, some would argue, at a corporate and government level too. This under saving has contributed to many families facing hardship during the current economic crisis. It is also one of the reasons small businesses are struggling to find banks that will lend to them to enable them to invest, as the major banks had accumulated too much debt and now need to recapitalise.

Why do we need an investment led recovery for green growth?

The challenge of climate change and the need for a low carbon transition is simultaneously throwing up a need for a surge in long term investment to renew our infrastructure, to reduce dependency on fossil fuels and develop a truly low carbon economy. If our economic recovery does not involve this investment, at a much higher level than previous recoveries, then the increased consumption to come will lead to higher use of fossil fuels and our carbon emissions will diverge dramatically from the path required to prevent dangerous climate change. A low carbon, investment led, recovery would, by contrast, ensure that future growth in consumption was decoupled from carbon emissions.

The UK needs to focus on the original role of savings in an economy, to provide the capital for investment. We need people to save more for their future and for a higher proportion of those savings to go into long term investments in infrastructure designed to build a low carbon transition. Otherwise the future we are saving for will be ravaged by climate change and subject to high and volatile fossil fuel prices.

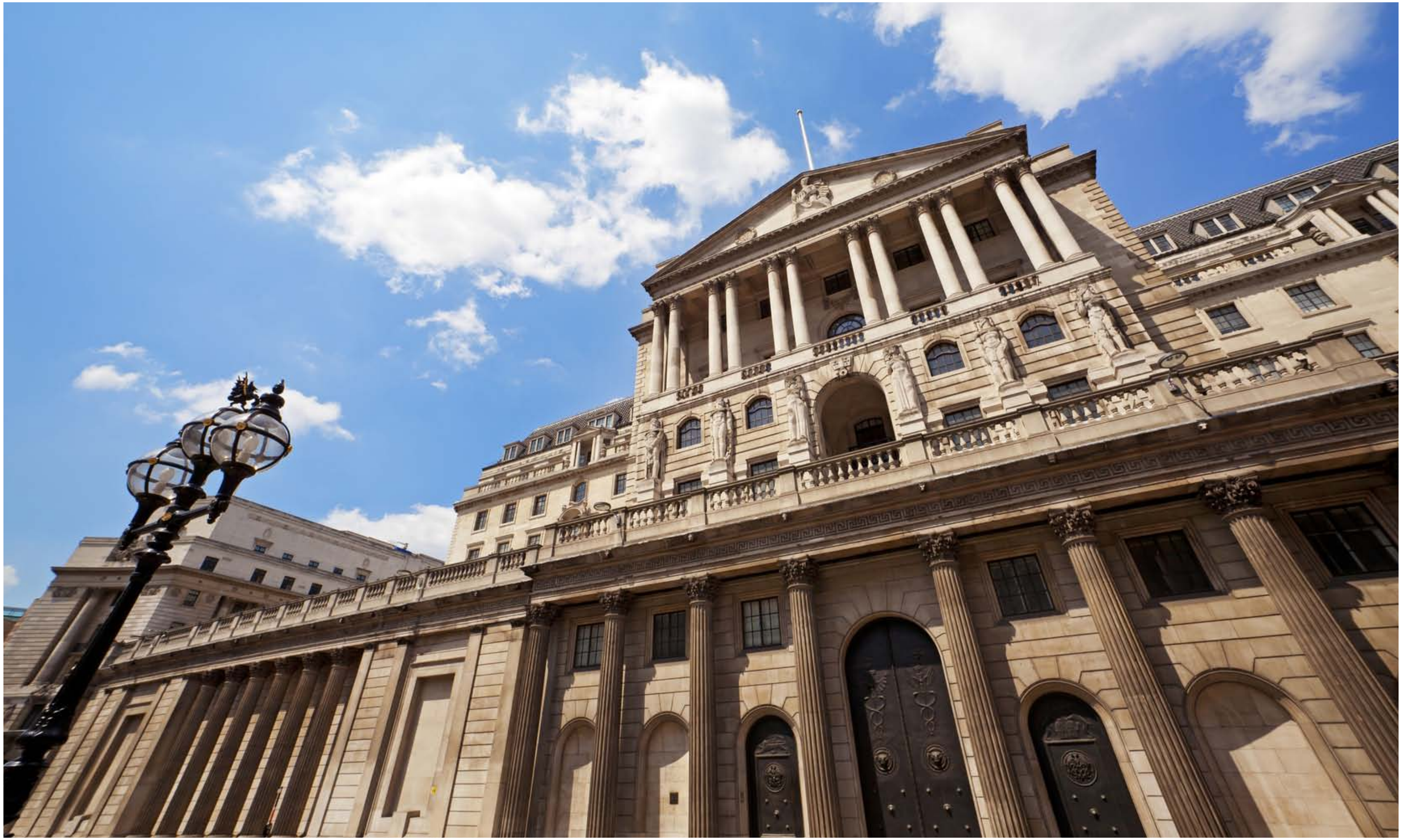
A new policy agenda

The government already grants considerable tax benefits for savings accounts, pensions, business investment and even property. In 2010-11 it spent over £30 billion on tax relief for savings and investments.[1] The private benefits for families who save or businesses that invest are clear, but there is surprisingly little analysis about the return the taxpayer receives for these subsidies.

"A low carbon, investment led, recovery would ensure that future growth in consumption was decoupled from carbon emissions."

We look at whether public policy measures can be used to create a virtuous circle of savings and investment in a sustainable economy, rewarding and encouraging savings and investments that provide long term benefits for the country as a whole. Can we rebuild the public trust in financial institutions? Can we use our savings wisely by offering incentives and regulation to steer more capital into assets that have clear social and environmental, as well as financial, benefits for the country? Can we make our savings work harder for our collective future?

2. The UK's broken savings and investment cycle



UK society does not save enough for its own future, either collectively as a nation, or across individuals and families. Economic growth has been driven by increased consumption compared to investment, and too much of the finance for this consumption has come from borrowing without countervailing savings being made in other parts of the economy.

Traditionally, people save to protect themselves from future falls in income either unexpected, through job loss or illness, or planned through retirement. In return the financial sector uses those savings to invest in companies, infrastructure and other value creating activities that deliver a return and pay the interest we receive.

However, the financial sector has suffered a failure of trust, much of it self-inflicted. The banking crisis, pensions and insurance mis-selling scandals and the image of a bloated financial services sector in general, has helped us all to lose touch with those twin purposes of savings and investment. So the UK has been doing less of both.

The finance sector has also become increasingly impatient as a user of capital. The short term return on investment has become collectively far more attractive for investors and companies alike, than the longer term investments that are sometimes required for an economy to function efficiently.

Finally, we all face the challenge of making the transition to a low carbon and climate change resilient economy, which will require investment in infrastructure, housing, transport and energy supply systems on a monumental scale. These investments are long term in nature and, in many cases, will not make the short term financial returns that the market conditions of today require.

Problems with UK saving culture

Britain has a well documented low savings rate. Whether for putting money aside for a rainy day, or ensuring sufficient pensions savings for retirement, the statistics show the UK has a very poor track record in comparison to our competitors. The OECD figures for percentage of household income going to savings have consistently placed the UK near the bottom of the league table. In 2008, the UK was the second lowest in the OECD, with only the US below us[2]. Other EU countries such as Germany, France, Spain or Italy have all had much higher savings rates. There has been a slight increase in UK savings following the credit crunch, the majority of which has been paying down debt and high mortgages.

The consequence of low savings for individuals has been a higher reliance on credit, which has contributed to the economic damage suffered in the UK as a result of the credit crunch and global financial crisis. For low and middle earners, lack of savings can mean that an unexpected fall in income or additional cost leads to additional borrowing, whether on a credit card, or from a short term lender, which increases interest payments and more prolonged income reductions. Research by the Institute for Public Policy Research (IPPR) found very low saving rates amongst low and middle earners. 40 per cent of families earning £20,000 a year have no savings at all, with a further 20 per cent only having up to £1,500 in savings.[3] The most recent 2011 savings survey from National Savings and Investment found that six million people (13 per cent) in the UK had no savings at all.[4]

"Short term return on investment has become collectively far more attractive for investors and companies alike, than the longer term investments that are sometimes required for an economy to function efficiently."

Policy makers and economists have become increasingly concerned by the trend of reduced savings, with the shortfall in pension saving seen as the most urgent, given the ageing population and likely increase in healthcare costs that will result. A succession of commissions has worked on the pensions issue over the past decade, with the Turner Report being the most comprehensive.[5] The forthcoming introduction of the National Employment Savings Trust (NEST) pension scheme, which will include 'auto-enrolment' with an employer pension scheme, is the highest profile policy intervention to come from the Turner Report, but others have been calling for more effort to restore the savings culture of UK citizens. In 2010, the Association of Independent Financial Advisors issued a white paper on rebuilding Britain's saving culture, in particular advocating the use of behavioural finance techniques rather than simple rational policies. The introduction of 'opt-out' systems for pension saving under the NEST scheme is one such intervention.[6] The Centre for Policy Studies has recommended the simplification of tax treatment between pensions and savings accounts to make long term saving more attractive to the public.[7] A campaigning website, SaveOurSavers.co.uk, has also been established to raise awareness of the impact of government policy on savers, and to advocate reform.[8]

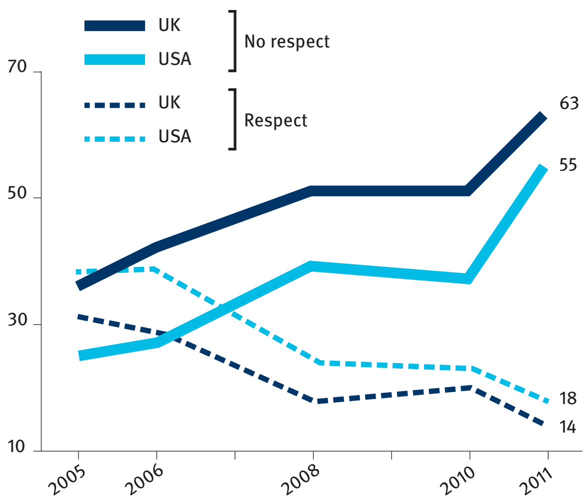
But, as well as the detrimental effect on the economic resilience of individuals and families in the UK, the low savings rate has a knock on effect on levels of investment. In his book and BBC series on UK manufacturing, 'Made in Britain', the economic journalist Evan Davis demonstrated the link between Britain's savings and investment rates. OECD figures show the UK invested, on average, 18 per cent of its national income in fixed capital from 1970 to 2008. Over the same period China invested 31 per cent, Korea and Japan 29 per cent and Germany 22 per cent.[9] All of these countries also had higher savings rates than the UK. That is not to argue that maximising saving is always good for the economy, but merely that the balance between saving and consumption in the UK is wrong and needs to be corrected.

Economists at the London School of Economics (LSE) have written about a glut of savings in the global economy, particularly being generated in China and other Asian economies. They argue that the UK should be attracting this capital for investment into our low carbon transition through a long term policy framework.[10] However, another report on global long term investment by McKinsey highlighted that countries such as US and UK should do more to increase their domestic savings rates if they want to have an investment led recovery, rather than a consumption led one.[11] They suggest that the large savings being generated in Asia are likely to be sucked back into their domestic economies as their own investment and infrastructure needs to expand and, indeed, that Asian governments are trying to reduce their own savings rates. If we are serious about rebalancing the UK economy away from over reliance on services to a rejuvenated manufacturing sector with higher exports, then investment must increase, and a higher savings rate would help make that happen by creating more domestic capital.

Public trust in the financial services sector is broken

At the same time as falling rates of saving and investment, the reputation of those institutions entrusted with our savings has also dropped considerably. Over a number of years, and largely due to its own performance and mistakes, the public reputation of the financial services sector has fallen. Nottingham University has run a Financial Services Trust Index since 2003, through questionnaires and interviews with a sample of the public. Its latest data shows that trust in the banking sector fell sharply after the financial crisis and has not recovered a great deal. Financial advisers receive the highest trust rating in the sector, and building societies also fare better than banks.[12] A more recent opinion poll from GlobeScan, found 63 per cent of the British public had "little or no respect" for banks, which is even higher than in 2008.[13]

Respect for Banks
"Respect" vs "No Respect", UK and USA, 2005-2011
Source: GlobeScan Radar (2011)



Another key finding of Nottingham University was that people's trust, particularly in their own bank, was in some ways 'forced'. As most people felt there was no choice but to keep their money in a bank, or maintain their pension contributions, they had to trust the professionals. This only really breaks down in the height of a crisis, such as the run on Northern Rock. Whilst the link in the public mind between trust in finance sector and whether or not they save is by no means direct, it will be hard for government policy makers to actively promote a saving culture without taking steps to simultaneously safeguard the integrity of the institutions which would manage the money.

High profile cases of mis-selling, coupled with the overall poor performance of pension fund investments have hurt the pensions industry. The Centre for Policy Studies cites a number of reports demonstrating the low return of managed pension funds. Over the past ten years, the average growth of pension fund assets has been 2.25 per cent, before costs. If that money had been simply deposited into bank accounts it would have grown by an average of 4.7 per cent.[14] Then there is the issue of the extremely high costs of the industry. The RSA pointed out in their study, *Tomorrow's investor*, that typical annual management fees for a private pension based on unit trusts, are 1.5 per cent which, when added up across the entire lifetime of the pension, can reach 40 per cent of the total amount put in by the saver, a staggering amount and far higher than other European countries, which shocked all of the members of the public involved in the researchers' focus groups.[15]

The financial crisis of 2007-08 has clearly damaged the reputation of high street banks but, even before, the issues of unfair charges, mis-selling insurance and closure of high street branches were already hurting the public image. On the specific issue of saving accounts, Consumer Focus made a formal complaint to the Office of Fair Trading about banking practices on interest rate setting for cash ISAs. They alleged that it was common practice by banks to attract customers with a high interest rate to a tax advantaged ISA, only to reduce the rate later on, hoping that customer inertia would mean most people were not likely to switch their account once set up.[16] Another opinion poll, commissioned by Triodos Bank, has shown a strong desire amongst the public to know what banks do with their savings. Just three per cent of people feel their bank is transparent about what they do with their savings and 85 per cent want more information about it.[17]

"the message received by the average saver is that long term financial security is best delivered by investing in an asset price bubble."

There is some evidence to show that the public have reacted to the banking crisis by shifting their savings to products offered by ethical banks, the most recent *Ethical consumerism report* from the Co-operative Bank recorded a 23 per cent rise in ethical finance products between 2007 and 2009.[18] This rise, however, is from a very low base. The Co-operative Bank itself has successfully expanded, merging with the Britannia Building Society. Triodos Bank has also grown, and other innovative financial institutions, such as the peer to peer lending site Zopa and the Charity Bank have all sprung up. Overall, however, Bank of England statistics on market share in savings show remarkably little changes from 2007 to 2010, with mainstream high street banks holding the majority of savings, and no significant shift to either ethical banks or even the building societies that remain mutual.[19]

In terms of consumer attitude to savings, the overwhelming feeling is that of confusion. Switching bank accounts is not high on most people's 'things to do' list. Research by AEGON into consumer attitudes towards long term saving showed a distinct bias towards property and buy-to-let as the best way to save for the future, based largely on the perception of ever rising property prices.[20] This in itself demonstrates how our financial system is failing to communicate the collective benefits of savings and investment, when the message received by the average saver is that long term financial security is best delivered by investing in an asset price bubble.

Short term investment culture in finance and corporate sector

A common feature of analysis of the financial sector and its impact on the real economy, has been the growing dominance of short termist investment strategies. Whilst there is a clear market function for some taking a short term view, through increasing liquidity for example, if the majority of investors are looking for very short term profits, then a great many companies with good long term prospects will lose out. The overall impact on the economy is likely to be detrimental, and long term sustainability risks, such as climate change will be completely ignored. The government has begun addressing this phenomenon with a consultation paper in autumn 2010, which has stimulated an independent review, chaired by Professor John Kay, although this is narrowly focused on equity shareholding, rather than the whole financial system.[21]

Senior commentators have been raising concerns about short termism for some time, foremost among them is Andrew Haldane, executive director for financial stability at the Bank of England. In a series of speeches over the past few years, he has expressed considerable concern at the impact of excessive short termism in the equity markets on the prospects for long term growth in the economy. He cites powerful evidence of the growth of short termism, even amongst long term investors, such as pension funds. In the UK, the average duration of an equity holding has fallen from five years in the 1960s, to two years in the 1980s, to seven months in 2007.[22]

There is also the growth of high frequency trading (HFT), where equity transactions are carried out in matter of milliseconds. Haldane quotes estimates that 30 to 40 per cent of all European equity trading might be accounted for by HFTs. A fair proportion of the capital being used for these trades will be from pension funds, whose ultimate investors are far more interested in a long term return based on economic fundamentals than the daily, or hourly swings of stock prices.

This short termist approach is also affecting the rest of the corporate world, as shown in a recent PricewaterhouseCoopers (PwC) survey of FTSE 100 and 250 executives, also cited by Haldane in his work. PwC asked the executives if they would prefer a £250,000 return tomorrow, or a £450,000 return in three years' time. The latter is clearly more profitable, but the majority of the respondents preferred the lower return immediately.[23]

"Andrew Haldane, executive director for financial stability at the Bank of England. He has expressed considerable concern at the impact of excessive short termism in the equity markets on the prospects for long term growth in the economy."

Professor Paul Woolley at the LSE makes a strong argument that the impact of the short term nature of the finance industry, coupled with the long supply chain of the investment industry, where pension funds employ agents to make most investment decisions on their behalf, explains the propensity of capital markets to be inefficient. This has produced the sort of asset bubbles and crashes that we saw back in 2008.[24] There is also a great deal of debate around how the fiduciary duty of pension trustees has been misinterpreted by fund managers, and the asset owners that employ them, as a legal duty to maximise short term returns, based on quarterly targets.

The recent report from Fair Pensions on the future of fiduciary duty argues very clearly that the current situation is not in the best interests of the investors, who for the most part, are ordinary UK pension holders.[25] This is the underlying point often overlooked in technical discussions about financial services: it is ordinary savers who are providing a great deal of the capital for the markets to invest or trade with. For the most part, those savers are putting money away for their retirement. They want a reasonable return, so they have a decent income later in life after they have finished working. Their core interest is in the long term, not the short.

The chief purpose of the financial system is to take those savings and invest the capital wisely to grow the economy and provide services to the current and future generations. This inherently long term function is being overshadowed by the ability of the financial services industry to create the wealth for itself, primarily through secondary and tertiary trading and ever more complex financial innovations. Pension funds are invested in a diversified portfolio of equity shares, bonds, property funds and other asset classes. The trustees of pension funds will contract this fund management role out to other organisations, who may also take advice from investment consultants. As the investment task is passed down a 'supply chain' the financial interests of the original pension holder can get lost on the way.

These conflicts of interest between 'agent' and beneficiary have been well documented and a number of organisations, including the OECD, the World Economic Forum, the UK Sustainable Investment Forum (UKSIF) and the Network of Sustainable Financial Markets, have all looked at the problems in recent years.[26] The most recent study by Forum for the Future , which serves as a very good summary of current knowledge, is *Overcoming the barriers to long term thinking in financial markets.*[27] This report shows that the barriers to long termism are now well understood but the debate over policy response is only just beginning.

Short termism also has an impact on the economics of climate change. If the prime motivation of most investors is to make a short term profit, they do not need to be concerned with the long term risks of climate change, or potential long term profits from low carbon investments, as long as the alternative fossil fuel stocks are more profitable today. This is well illustrated by the recent report from Carbon Tracker, which has looked at the market valuation of the world's fossil fuel companies, usually based on all the reserves owned by those companies.[28] Only 20 per cent of the total global fossil fuel reserves need to be burnt to push the world into dangerous climate change, yet the market valuation of the companies is still based on the potential revenue generated by all of the reserves being used. Individually, these are perfectly rational valuations, but at a systemic level the economic damage created by climate change would be far greater.

"Only 20 per cent of the total global fossil fuel reserves need to be burnt to push the world into dangerous climate change, yet the market valuation of the companies is still based on the potential revenue generated by all of the reserves being used."

Another factor, illustrated clearly by the Carbon Tracker report, is that investing in equities listed on the London Stock Exchange is not the same as investing in UK business. In fact the Exchange is the financial home for a large number of fossil fuel companies such as BP, Shell, Rio Tinto and Anglo American. Adding up the total amount of fossil fuel reserves owned by companies listed on the Exchange, almost 20 per cent of all the fossil fuels in the world (based on CO_2 equivalent) are owned and traded in London, compared to UK annual emissions which are roughly two per cent of the global total.[29] This means, of course, that a large proportion of all of our pensions savings are invested in fossil fuels, the authors estimated as much as 30 per cent.

Low carbon infrastructure investment gap

The final challenge for our economy in the next few decades is the enormous levels of investment required to transform our energy, transport and built infrastructure to maintain energy security and deliver a low carbon economic transition. There is broad political and economic consensus about the scale of this challenge, even if there is less agreement about how to go about it. The UK has targets to reduce greenhouse gas emissions, compared to 1990 levels, by an average of 22 per cent (2008-12), 28 per cent (2013-17), 34 per cent (2018-22), and 50 per cent (2023-27), as set out in the carbon budgets recommended by the Committee on Climate Change, and now accepted by the government.[30] Such reductions will require major infrastructure investments across the entire economy, at levels we have not previously sustained. The returns on infrastructure investment are by definition long term in nature, so the impact of an increasingly short term focused investment community is strongly linked to the prospects for a low carbon transition.

The low carbon economy is necessarily more capital intensive because of the nature of renewables and energy efficiency, where the costs occur in the infrastructure rather than in fuel. Ernst & Young estimated in 2010 that the UK would need £450 billion of capital investment between 2010 and 2025.[31] Other studies, which included related supply chain needs, place the figure higher at £550 billion by 2020.[32] These levels of capital investment in infrastructure are far higher that the UK has managed in recent years, so the need for an investment led recovery is reinforced by the climate challenge. The London School of Economics has analysed this investment need to demonstrate that a low carbon economy would be good for growth and jobs in the UK. In particular, investments in the built environment are likely to create many jobs.[33]

3. Three building blocks for sustainable, investment led, recovery

Can we turn the threats outlined above into opportunities for a new economy that saves more, invests more, and makes its judgements on savings and investments based on long term factors? This would create a society more resilient to climate change and make the transition to a low carbon economy possible. It will not be a quick process but the foundations of such an economy will need three important building blocks.

First, we need to restore public trust in financial institutions to the degree that the savings culture is revived in British society. A higher rate of savings in the UK would help us adjust to the challenge of an ageing population and increase the pool of capital available for investment, reversing the dependence of prosperity on ever increasing consumption.

Second, we need to find ways to give greater reward to long term investment, reversing the trend of short termism that has undermined productive sectors of the economy and provide a greater stability for business and innovation.

Finally, we need a higher proportion of the increased savings and investments to flow towards the vast range of activities that increase energy security, reduce carbon emissions and enhance social and environmental well-being, as well as provide financial returns.

1: Restore saving culture to the UK

If the savings rate in the UK could be brought back to the sort of levels enjoyed by other EU countries, or even those the UK had in decades gone by (UK savings rates were 8.9 per cent during the 1980s and 1990s but only 4.3 per cent in the 2000s)[34] then the social and economic benefits would be considerable. A higher proportion of individuals would be more financially resilient, so less reliant on benefits. Any increase in the proportion of income saved would result in a reduction of consumption, perhaps reducing some of the greater excesses of materialism in our society. Certainly we would see a reduction on reliance on credit for funding such consumption. Assuming the savings were being used to fund capital investment, and not simply sitting under the mattress, then the money would still be used for improving the productive capacity of the country, growing businesses, building infrastructure and investment in the built environment. All of this would help to create more sustainable consumption in the future.

"A higher rate of savings in the UK would help us adjust to the challenge of an ageing population and increase the pool of capital available for investment, reversing the dependence of prosperity on ever increasing consumption."

If the Vickers reforms, ring fencing retail banking from more risky investment side of the businesses, go ahead as planned, then a boost to UK savings will also help to make the banking activities within the ring fence more commercially attractive, as greater levels of capital will be available.[35] Maybe there could be a resurgence of mutual lending and other finance business models that were lost under the last wave of deregulation of finance, as lamented by John Kay and others.[36] In a sustainable economy we would want to see this shift from consumption to savings matched by a rebalancing of the economy, driven by a greater focus on long term factors from the investment community.

2: Encourage longer term focus for investments

The majority of our savings are in pension schemes, with the return on capital not due for decades after deposits are made. This supply of capital should be the ideal pool from which long term investing is financed, making the citizen investor a powerful owner of equity in UK listed companies, ensuring their long term interests are at the centre of corporate governance. As described earlier, this is not the case, as the capital in our pension funds is managed through a series of agents who are frequently measured against a quarterly performance benchmark. In a more sustainable economy, our pension savings would be invested and managed with the long term interests of the pension holder at the heart of the strategies. Active asset owners would be the norm and the values of responsible investment would permeate throughout the City. Fund managers would be rewarded based on far more sophisticated benchmarks of financial success over periods of years, not months.

Some analysis of the benefits of long term investing for the global economy has made the explicit link between taking a long term approach and the needs of a low carbon economy. The World Economic Forum's recent report, *The future of long-term investing*, cited the greater propensity of long term investors to take into account externalities in their investment decisions, and understand the impact of those externalities on other parts of their portfolios, as a public benefit of encouraging more long term investment.[37]

"Analysis of the benefits of long term investing for the global economy has made the explicit link between taking a long term approach and the needs of a low carbon economy."

The potential benefits would be great in terms of economic stability, with a reduction in the number of asset bubbles created by markets and the ability of businesses to manage for long term value creation, rather than constantly worrying about short term share price fluctuations. However, short term economic recovery may be slower than if a consumption led strategy is pursued by government. The question is whether our political or financial systems have the sort of patience required.

3: Attract more savings and investments into low carbon and social enterprise

As longer term factors and climate change risks become better understood by the financial community, then a higher proportion of long term investment would be made in low carbon technologies and other sustainable businesses. Banks would begin to measure their lending to the clean technology sectors and promote the size of that lending compared to that in the fossil fuel industries. Pension funds and other institutional investors would also find ways in which to actively engage in the growth of the low carbon economy, whether through green bonds, low carbon infrastructure funds or other new products. Such shifts in investment patterns will not come about simply through one or two policies but only in response to a coherent long term policy framework, for which many institutional investors have been calling for some time. But it will also be with the grain of public opinion. Surveys from the socially responsible investment community have shown that over half of the public are willing to save and invest their money in more socially responsible ways.[38]

Foundations for a sustainable recovery

These three building blocks could form the sound foundations for a more balanced and sustainable growth path for the UK than we have experienced over the past few decades. Together they form a virtuous circle of higher savings, lower consumption and higher investment with sights on the long term, providing better economic prospects for the future. Much of this will have to be delivered through individual decisions, changes in cultural attitudes and business innovation.

The question for the next chapter is: to what degree can public policy create the framework to prevent the market failures which tempt both consumers and investors towards so-called 'jam now' strategies, piling up debt and under investing in the future? To quote the economist Diane Coyle, can we create an economics as if the future really mattered?[39]

4. How to encourage sustainable savings and investment

The government already has a number of policy instruments designed to encourage saving and investment. Many of us are familiar with the Individual Savings Account (ISA), which allows for a set amount each year, to be deposited into a savings account or equity fund, to earn interest free of tax. Similar tax breaks are offered for certain forms of private equity investment and venture capital. The Enterprise Investment Scheme (EIS) and Venture Capital Trusts (VCT) allow tax free investment up to a certain annual limit.

The largest subsidy for long term savings comes in the form of Pension Tax Relief, where income saved in a pension product is deductible from tax in the year it is saved. As well as tax incentives, the government also issues its own saving products through National Savings and Investments (NS&I). Finally, given that many of us see property investment as a form of saving, some might argue that the capital gains tax regime also has an impact on saving.

The latest figures show that the government spent £30 billion on subsidies to saving and investment in 2010-11, rising to nearly £40 billion if tax breaks on the sale of residential property are included.[40]

Here, we will look at whether there are ways to redesign these policies so they continue to encourage saving, whilst also delivering a greater return for the taxpayer in terms of benefits to the environment, social cohesion or long term economic stability. Can we apply a new principle that, in return for tax relief and implicit subsidy, savers and investors should demonstrate a contribution to the public good? First, we look at what long term policy reforms might be needed if we followed such a principle through to its logical conclusion (options 1 to 4 below). Second, acknowledging that such reforms would take time to work out and implement, we explore how government could experiment with the principle's feasibility by introducing some shorter term limited policies designed to see how the savings and investment markets react (options 5 and 6 below).

Long term policy reforms

Far reaching reforms, introduced over a number of years, would be necessary to follow the principle of granting a tax subsidy only on the condition that the public good and long term social, economic and environmental interests of both the saver and the taxpayer were considered. Areas of change we have highlighted below are pension tax relief, individual savings accounts and capital gains tax in relation to domestic property.

Pension tax relief

By far the greatest subsidy given to savings and investment in the UK is pension tax relief. Allowing pensions investment before income tax or national insurance contributions are calculated costs the Treasury £30 billion according to government figures.[41]Given the role of pension funds in underpinning the financial system and capital allocation across equity markets, it is reasonable to ask whether the taxpayer subsidy should come with strings attached to encourage investments on a more long term and responsible basis than they are at the moment. Such conditions could be seen as the taxpayer's equivalent of the fiduciary duty. Are the subsidies to pension funds invested in a way that is in the long term interests of the taxpayer who is providing them? Research has shown that much of the subsidy, at the moment, disappears into fees and charges and what is left has gone disproportionately to higher rate taxpayers with very large pension contributions.[42]

"Given the role of pension funds in underpinning the financial system it is reasonable to ask whether the taxpayer subsidy should come with strings attached to encourage investments on a more long term and responsible basis"

Mainstream debate over the future of pension tax relief has centred around how much of it is taken up by higher rate taxpayers. Changes introduced by the last Labour government and the present coalition have made the system more equitable, by reducing the maximum amounts that can be saved tax free in any one year, and reducing the availability of tax relief at the higher rates. However, the idea of looking at linking tax breaks to long term or responsible investment has been mooted by, amongst others, Forum for the Future, in speeches from Andrew Haldane, a think piece by Richard Murphy of Finance for the Future and in Network for Sustainable Financial Markets blog posts.[43] The ideas are in their infancy and, below, we try to flesh out in a little more detail how such reforms could be envisaged.

We hope it will stimulate debate and new thinking from others.

Option 1: Specify 'responsible investment' conditions for the eligibility of pension tax relief

Concern about myopia and over emphasis on the short term by the investment community is one shared by a broad spectrum of commentators, not just those interested in sustainable development. It is also far more likely that an investment community focused on the long term would be factoring climate change, low carbon and sustainability issues more clearly into its asset management. So could a condition for receiving Pension Tax Relief be initially tied to some measure of a long term, or 'responsible' approach?

Britain already has a voluntary code of good practice to encourage good corporate governance and investor engagement. Any investor taking climate change or sustainability seriously would already be leading exponents of these pre-conditions. The Stewardship Code, overseen by the Financial Reporting Council, sets out a series of investor engagement principles to which signatories state they will adhere. The code has its critics, some dismiss it as a 'tick box' exercise that has little bearing on actual investment decisions, whilst many asset owners have not signed up, either because they see it as irrelevant to their decision making, or as an over burdensome requirement that would hurt their returns. A similar international code has been developed by the UN. Its Principles of Responsible Investment (PRI) are more explicit about environmental and social issues and it has signed up a growing number of large global pension funds.

Requiring a pension fund to sign up to the Stewardship Code or PRI before any pension tax relief is awarded, would be a strong signal. The pressure would come from the pension holder themselves who would have a high incentive to switch to providers who are SC or PRI compliant, but the industry could be expected to pre-empt such switching by signing up.

"Investors taking a genuine long term view of their portfolios are more aware of climate change risks and more likely to invest in infrastructure, one of the key components of the low carbon transition."

Placing this condition on tax relief would make the Stewardship Code, or similar code of practice, itself a far more powerful mechanism, so simultaneous efforts should be made to improve the code, and to find more meaningful metrics by which to establish compliance and more transparent reporting requirements. For example, a few years ago a voluntary initiative was tried with an accreditation scheme for asset fund managers on environment, social and governance (ESG) issues. Institutional investors were asked to sign up to ensure that five per cent of their assets were managed by companies which had ESG accreditation. Asset managers signed up in their droves, hoping to attract more business, but asset owners were not interested, fearing that the burden of compliance would undermine their returns. If such a rule were applied to a strengthened Stewardship Code, linked to a condition on pension tax relief, then far higher take up could be expected. There would be further benefits in terms of greater transparency of investor behaviour revealed through the improved reporting requirements of the Stewardship Code, which would be needed to prove eligibility for tax relief.

The impact of such a condition on sustainable investment would be indirect, but it tends to be those institutional investors, such as the large public sector pension funds, which have signed up to responsible investment codes, that are the ones taking the greatest interest in the low carbon economy. It is they who sign up to international statements calling on governments to take more action on climate change and, perhaps more significantly, they are the main early purchasers of green bond issues by the World Bank and the European Investment Bank. It is also fair to say that investors taking a genuine long term view of their portfolios are more aware of climate change risks and more likely to invest in infrastructure, one of the key components of the low carbon transition.

Option 2: Increase the length of equity holdings by pension funds with tax incentives

The analysis by Andrew Haldane at the Bank of England, amongst others, showing the ever decreasing length of time that institutional investors hold their shares, is the clearest evidence of a growing short termist approach to equity. Could tax incentives be used to reverse this decline? If they could then, as more investors held stakes for years at a time, greater interest would be shown in the long term prospects of the businesses being invested in and long term risks, such as climate change and sustainability, would also be taken more seriously. Paul Woolley at the LSE has pointed out that pension tax relief is given in part as an incentive for investment in the economy, and there is a specific clause in UK law that states tax exemption should be withdrawn for any fund that is deemed to be 'trading' rather than 'investing'. No definition has been established for this, but Woolley suggests that funds should be restricted to an annual portfolio turnover of 30 per cent.[44] That translates into an average equity holding being three years, compared to only seven months now.

One approach that might shed some light on this rarely examined piece of law, could be a legal challenge to ask whether the government is implementing tax relief appropriately.

Another tax route to a similar outcome would be to graduate capital gains tax on investment funds, so that there is a lower tax on the investment return on a primary activity (ie buying shares directly from the company issuing them) than on secondary trading of shares (buying and selling on the stock market).[45] This, however, may become complex, and would undoubtedly stimulate a great deal of innovation in the tax avoidance industry.

Tax free allowances for Individual Savings Accounts

In 2009-10 £45 billion was invested in Individual Savings Accounts (ISAs), £32.5 billion in cash accounts and £12.5 billion in equity funds.[46] These figures have been gradually increasing since ISAs were introduced in 1999, when the total saved in them was £28 billion (£12 billion in cash and £16 billion in equities). From April 2010, any individual can save up to an annual limit of £10.200, of which £5,100 can be held in cash, the interest earned from these accounts is tax free.

The ISA has become one of the most popular ways to save, with HMRC statistics showing that there were 15 million subscriptions last year alone,[47] but the system is not without its critics. Some doubt the extent to which the tax incentive encourages those people to save, who otherwise would not have done, posing the question that the subsidy might be a deadweight cost to the Treasury.[48] As mentioned previously, Consumer Focus has also questioned whether the interest rates offered by ISAs properly reflect the tax incentive.[49] If the interest rates are lower than they should be, then this in effect means that the bank is receiving the benefit, rather than the saver. Amidst these criticisms, one can legitimately ask whether the government should be looking for an extra public benefit from the tax relief, ie the encouragement of more social and environmental investment.

The recent growth in ISA subscriptions has been in cash accounts, both in terms of the number of people involved (12 million in 2009-10) and total savings (£32.5 billion).[50] If there was a way to engage the cash ISA market in sustainable investment then it could be a far more powerful lever, both as a means to involve a wider section of the public, but also in total investment terms. But this is far more complex in terms of defining what we mean by a green or sustainable cash ISA. For, when you save in a bank or building society account, the money simply goes into

"Should the government attach more stringent conditions to accounts that are tax free?"

the bank's consolidated fund for lending, it doesn't sit in a special earmarked fund. The only institutions to currently have green or social cash ISAs are those such as Triodos Bank or Charity Bank, which only lend to those sectors. The options open to policy makers to encourage sustainable cash ISAs hinge on devising some way to prove that the money saved is actually increasing finance available to those sectors.

Option 3: Establish sustainability or transparency criteria for all ISAs

Given the popularity of the ISA account, the government has a certain amount of leverage with savings institutions in granting the clearance for them to carry an ISA account on their books. It is a powerful marketing device to attract savers, so should the government attach more stringent conditions to accounts that are tax free? Should the banks that have made irresponsible investments with their customers' savings have the same rights to attract more customers with the aid of a subsidy, or should that right come only with a responsible investment strategy?

There are codes of practice designed to encourage responsible investment, such as the Stewardship Code or the UN's Principles of Responsible Investment, previously mentioned, but these are primarily aimed at asset managers and investment, rather than banks and lenders. The government could require all institutions that offer ISA accounts to sign up to these or some other 'responsible investment' code of practice designed for lending institutions. This could apply to stocks and shares ISAs fairly readily but, as such a code does not currently exist, and smaller banks and building societies would face a higher administrative cost, it might not be the most practical method for cash ISAs.

"All banks could be required to be transparent about the sectors they lend to as a condition to allow them to sell ISA products."

Given the current limited size of the clean technology and social enterprise sectors, creating a condition that all cash ISA accounts should lend directly to sustainable companies could hit against the problem of a lack of projects and companies to lend to, in the short term at least. Although the more established companies do have a need for equity and debt finance, so this market will grow. But, if there were ways in which banks and building societies could demonstrate they were increasing their lending to such sectors, then some metrics, or even targets, could be developed by which to link ISA eligibility. In the first instance, all banks could be required to be transparent about the sectors they lend to as a condition to allow them to sell ISA products. In time this could evolve into agreements to increase the proportion of their lending to clean technology, or companies that were deemed Green Investment Bank(GIB) or Big Society Capital (BSC) compliant. This may be hard to regulate and could prove complex, which is why we propose starting with a simple transparency rule. Any withdrawal of ISA accounts would only apply to new subscriptions so existing savers would not be penalised retrospectively.

Property tax and capital gains

To many people the ownership of property is a form of saving and investment. Based on a rising housing market, many people have seen the equity in their homes increase over and above inflation.[51] The assumption is that when they retire they may move to a smaller property and the increase in the value of their home will be cashed in by selling the house. Others will pass this wealth on to their children. The wealthier may also invest in second or third properties, which are rented out and provide an extra income, as well as the asset itself. This form of saving also receives a tax incentive as any capital gain made from the sale of property, if it is your main residence, is exempt from capital gains tax.

Tax experts and campaigners have begun to highlight the illogical and potentially regressive nature of this particular tax break. The Mirrlees Review of the UK tax system, run by the Institute for Fiscal Studies, made it clear that it would be more economically efficient for the capital gain made from the sale of domestic property to be taxed like other capital gains, whilst recognising the political barriers to such logic are great.[52] Shelter, the housing charity, also believes that the taxation of property distorts the market in favour of owner-occupiers over those in rented property, and as such has contributed to the housing price boom. They recommend that capital gains tax (CGT) should be applied to all properties including the main residence, on grounds of reducing distortion in the housing market and removing the tax avoidance by those who classify a second home as their principal private residence to reduce their tax bill.[53]

Britain has a serious housing problem, both in terms of supply, but also the quality of housing. In particular, we have very poorly insulated homes which require a great deal of energy to heat to an adequate standard. Successive governments have sought to encourage home owners to invest in the energy efficiency of the building stock, to reduce fuel poverty and the greenhouse gas emissions associated with domestic heating. One of the current government's flagship environmental policies is the Green Deal which is designed to stimulate investment in energy efficiency.

Option 4: Make the exemption of residential property from capital gains tax dependent on energy efficiency improvements to the fabric of the building

According to latest HM Treasury figures the exemption of the main residence from CGT costs the tax payer £9 billion. A house will often exist for 100 years or more and over time the needs of society change. Arguably an energy efficient home will become more and more important as fuel prices rise and the need to reduce emissions to prevent climate change gets ever more urgent. If the taxpayer is giving a property owner a tax break on any increased value of their asset, could we legitimately seek some investment in the quality of that asset for the public good, such as improved energy efficiency?

"If the taxpayer is giving a property owner a tax break on any increased value of their asset, could we legitimately seek some investment in the quality of that asset for the public good, such as improved energy efficiency?"

The complexities of such a condition would obviously need to be addressed, but as we now have an accepted methodology for rating a house for its energy efficiency in Energy Performance Certificates (EPC), perhaps CGT exemption could be granted only for properties over a certain EPC band level?

The government has recently announced that the private rented sector will have to upgrade the energy efficiency of its stock by stating that it will be illegal to rent out a Band F or G property by 2019. The same principle could be applied to CGT exemptions to give property owners plenty of notice to make the necessary investments.

Such a measure may stimulate higher levels of investment, and may even help the EPC rating become a more important factor in the valuation of the asset itself. The Royal Institute for Chartered Surveyors recently issued guidance to its members stating that sustainability factors should be taken into account in valuations.[54] A change in tax law would reinforce this guidance.

Shorter term policy options

The four options above could not be introduced overnight, and would need considerable development to implement them in full. However, there are ways in which the principles behind them could be tested and encouraged by the tax system, with smaller policy changes in other parts of the savings and investment market. We recommend such changes could be introduced while conducting the wider debate around the conditions that should be applied to larger subsidies on savings.

Ultimately, any tax advantaged savings or investment product should be required to demonstrate the benefits to the wider economy, society and environment to justify a subsidy. An interim measure, however, could be to grant a temporary additional tax advantage to those investors who are first movers in demonstrating wider benefits. The differential in tax treatment could be an extra, temporary, subsidy until the conditions apply to all tax relief, or they could be implemented in a revenue neutral fashion, effectively reducing the tax relief for mainstream products to fund a slightly greater tax advantage for responsible investments.

Such interim measures would have two purposes. First, to reward early movers and, second, to allow exploration and development of the methodology by which investors should prove they are creating value to society.

Incentives for private sector green stocks and shares ISAs

Option 5: Extend the annual ISA savings allowance by £3,000 for additional money invested in green or social stocks and shares ISAs

If individuals were allowed to save an extra £3,000 a year tax free for investments in green or social ISAs that would be an additional incentive for sustainable savings. This incentive may encourage extra saving, or perhaps divert money into sustainable investment that would have otherwise gone into a mainstream pension fund. If the latter were the case then any tax revenue lost from the subsidy may be offset in the Treasury by a reduction in pension tax relief taken up.

"If individuals were allowed to save an extra £3,000 a year tax free for investments in green or social ISAs that would be an additional incentive for sustainable savings."

This idea was promoted by the Conservative Party before the 2010 election, and has also been recommended recently by the Aldersgate Group of businesses and NGOs.[55] It would operate in a similar way to the long standing tax incentive offered in The

Netherlands for money invested in Green Funds, which has levered €7 billion.[56] It would be an explicit subsidy for sustainable investment over and above existing savings incentives and, as such, a clear government endorsement and encouragement for those products.

On the face of it, it could only be claimed by individuals who have already exceeded their annual ISA allowance, there would be a limit on who could receive this extended maximum ISA allowance, and it would be the relatively well off. Such a structure would also place a de facto limit on the amount of investment that could be attracted into these particular sustainable savings products. According to 2009-10 statistics, the average equity ISA subscription was over £4,000, and over three million people subscribed to such funds[57], so the number of people who invest up to their limit might be, say two million in total. Of course there is no way of knowing if they would then be able to invest up to the extra £3,000 green ISA limit, but it puts a cap on possible investment at £6 billion and, given that the sales of equity ISAs have remained static ever since their launch in 1999, the potential is probably considerably less than £6 billion. However, given that the total ethical investment market was £11 billion in 2010[58], this is still a reasonably significant amount.

A way of enabling the green ISA limit to be accessed by a higher proportion of savers would be to make some changes to the eligibility criteria for green ISAs, compared to regular ones. Some growing clean energy companies, for example, have found more innovative ways to raise capital through bond issues. Ecotricity, the renewable energy supplier, issued a green bond last year and raised £10 million, and it plans further bonds during the next year.[59] Whilst such investments are higher risk, it could be possible to allow similar investments to qualify for green ISAs. Such flexibility could allow future green savings products to be given a head start in the market, such as allowing individuals to invest in the Green Deal, through the creation of a Green Deal Mutual, proposed by Ben Caldecott at Climate Change Capital.[60]

"Some growing clean energy companies, for example, have been finding more innovative ways to raise capital through bond issues."

Another complicating factor is how to set credible and meaningful definitions for what qualifies an account as a green, sustainable or social ISA. The market for socially responsible investment tends to have three different types of fund. The traditional ethical fund is negative screened, to take out certain sectors like tobacco or arms. More recently there are those which are positively screened, investing specifically in low carbon and clean technology companies. The third category invests in the 'best in class' for social or environmental issues across mainstream sectors. The latter can be accused of greenwash, in that they may well buy stocks from oil and gas companies, for example, but choose those with the lowest carbon footprint. However, the more exclusively cleantech funds may well be higher risk as the pool of companies they can invest in is much smaller.

The debate over which is better will doubtless continue for some time, but there is no need for this to derail an early introduction of green ISAs, as other parts of government are now coming up with criteria for social investment from Big Society Capital, and for environmental investment from the Green Investment Bank. Ultimately the simplest criteria for green or social ISAs would be for the companies or projects to be compliant with the requirements of these two institutions. Another alternative could be to set a percentage of the fund investment in clean technology.

The impact of this small incentive on the market for sustainable savings and investment would usefully inform the thinking about further fundamental reforms to the tax allowance for cash or equity ISAs.

Tax breaks for capital investment

An important part of the government's growth strategy is to encourage capital investment at this stage in the economic cycle. For those investors with more capital at their disposal than the ISA limits, other tax efficient investment vehicles are available. The Enterprise Investment Scheme (EIS) and Venture Capital Trusts (VCT) are designed to encourage equity investment in start up companies, often in technology and manufacturing where there are acknowledged finance gaps and market failures. These policy instruments are not so much designed to encourage people to save as to steer those with excess income to invest in UK industry.

Investors who take advantage of these policies are sophisticated, likely to be receiving professional advice on where to place their money and, as a result, are more influential in the investment world than average savers. If Britain wants to lead the global low carbon transition, then we need these investors to understand sustainability and to be stimulating rapid growth in clean technology and social enterprise. An extra tax incentive for these people to look at sustainable investments first is consistent with the desire to stimulate green growth at the heart of the economic recovery. It also raises awareness at the leading edge of the investment community, which could lead to faster penetration of these sectors into the mainstream.

"These policy instruments are not so much designed to encourage people to save as to steer those with excess income to invest in UK industry."

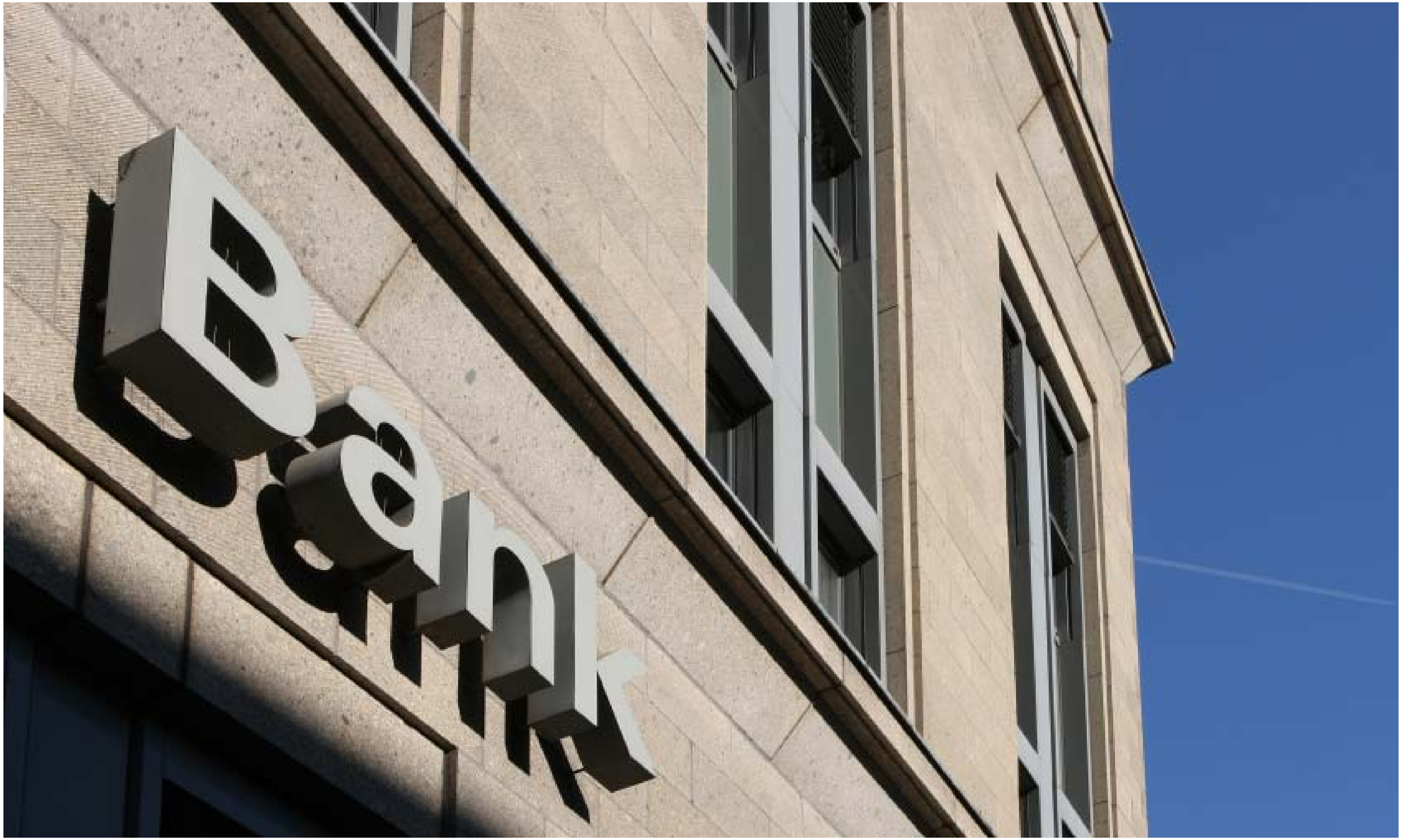
The Labour government had some success making public venture capital investments in low carbon technology, first through the Carbon Trust and then the UK Innovation Investment Fund. These initiatives rely on government making direct investments, albeit through an independent investment company, in specific companies. However, a simple tax incentive would allow the market to pick the companies against broader sustainable criteria.

Option 6: Increase annual tax free capital investment limits for sustainable companies

Currently, investments in VCTs and EIS can be made each year and the income generated from those investments will be subject to tax relief upon maturity, which is usually a minimum of five years. Transform UK, a coalition of businesses and NGOs campaigning for a low carbon transition, have suggested that for investments made in clean technology companies the limit could be set higher than for other sectors, thus attracting more investors.[61]

At the time of the last Budget, there was a proposal for any company eligible for energy feed-in-tariffs (FiTs) to be exempted from EIS and VCT, on the grounds that there is sufficient incentive for investment through FiTs. There was considerable concern that a number of community level renewable projects would fail if this restriction was put in place, and the government has now allowed community renewables projects to retain VCT and EIS eligibility. Given the role for both the Green Investment Bank (GIB) and Big Society Capital (BSC) to provide leverage for private investment, it would make sense to ensure that other tax incentives complement these financial institutions by creating greater tax incentives for GIB and BSC compliant projects. If the markets for such capital grow significantly in response to the incentive, then this could lead to the tax incentive being restricted to those investments which provide public as well as private benefits, as discussed in relation to pension tax relief earlier.

5. Next steps to a new agenda



There needs to be a far greater understanding amongst the saving public and policy makers about how money invested is ultimately deployed. Whether it is transparency from banks over their lending portfolios, or the extent to which pension funds grow through investment in the real economy or trading financial instruments in the markets. The saving public have a right to know. This could be a way of turning the current, understandably negative, discourse around financial services, now catalysed by the Occupy Movement, into something more positive and forward looking. Crucially this debate needs to shift from the City, where most of the knowledge currently resides, into both Westminster and the media.

"There needs to be a far greater understanding amongst the saving public and policy makers about how money invested is ultimately deployed."

Environmental and social organisations must play their part in actively promoting and campaigning for their members and supporters to question how their savings and investments are used, and encouraging them to make proactive sustainable investments.

Green Alliance believes there is a significant new political agenda to be created around this topic. Policy makers, the public and the financial services industry all need to adopt a new principle that, in return for tax relief and implicit subsidy, savers and investors should be able to demonstrate a contribution to the public good.

This principle, if followed, would manifest itself in some fundamental policy changes over the next few years:

- Favourable tax treatment of pension contributions and private equity investments, such as Venture Capital Trusts, should be reformed in ways that would require proof of responsible investment and asset management that genuinely reflects the long term interests of pension holders, and taxpayers.
- Banks and building societies should only be eligible to offer tax free ISA savings accounts if they can prove their responsible lending practices, including far greater transparency of the types of economic activities supported by their lending
- The exemption of residential property from capital gains tax could depend on proven energy efficiency improvements made to the fabric of the building during the period of ownership.

Such changes could not be carried out quickly, but the government could explore the feasibility of putting the principle into action by introducing some early, interim measures to see how the savings and investment market reacted:

- Grant an extra £3,000 ISA allowance for individuals to save in green or social stocks and shares ISAs, including the extension of the ISA eligibility to include corporate green bonds.
- Increase the investment limit for Venture Capital Trusts and Enterprise Investment Scheme funds which invest in clean technology or social enterprise.

This pamphlet has looked at the issue of the sustainable economy and green growth through the lens of the savings and investment cycle. Green Alliance believes this to be consistent with the government's green growth and Big Society agendas. The innovations of the Green Investment Bank, Big Society Capital, and the Vickers Commission could be built upon by exploring further ways to encourage investment for social, environmental and economic progress. This also chimes with the Labour Party's growing theme of the moral economy.

Taking the debate forward will require action on a number of levels: politics, citizen engagement, NGO awareness raising, financial innovation and policy making. There is great potential in harnessing the nation's savings to build a long term future. Using the leverage of existing tax benefits could be a way to restart the UK's savings and investment cycle on a more sustainable path, leaving the debt fuelled, consumption economic model behind.

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