

## ***Shaping a stable pensions solution:*** **Should state pensions be contributory or universal?**

On Thursday 14 July 2005 the PPI and the Nuffield Foundation held the third seminar in the *Shaping a stable pensions solution* series at the Nuffield Foundation.

Around 30 people attended the seminar, which was chaired by Richard Brooks (Research Director, the Fabian Society).

Alison O'Connell (Director, PPI), described the evolution of the contributory versus universal debate in the context of the basic state pension, and presented the key findings from the background paper to the seminar.

Dr Susan St John (University of Auckland), provided evidence from New Zealand in the paper *What can the New Zealand experience of universal pensions offer the United Kingdom debate?*

Three discussants gave contributions to the debate before questions and contributions were taken from the floor.

Please note that the PPI has not checked any facts referred to in the following, and may not agree with the opinions expressed.

**Frank Field MP** noted that:

The debate concerning a residency pension must be considered in the light of the recent London bombings, which may strengthen feelings both that citizenship needs careful definition, and that people should not get pension for nothing.

There is no need for reform to take place quickly, as the recent introduction of the Pension Credit means that there is not an immediate problem of pensioner poverty (although Pension Credit should have a shelf life to avoid undermining saving).

For the first time therefore a major pension reform has been decoupled from the need to help today's poorer pensioners. The Government

needs to come to a decision soon on what that long term reform should be (which will put the shelf life on Pension Credit) but, because today's pensioner poverty is being dealt with by Pension Credit, it can allow the long term reform to build up over time.

Any debate considering contributory against universal should not confuse design problems in the existing contributory system with what the ideal contributory system would look like in total, with more obvious reward and recognition of valuable contributions to society.

Reform cannot be purely technical – it has to work in the prevailing political structure and draw on what the public believes will endure.

An element of funding of a contributory pension may give a greater degree of comfort than relying on the generosity of future taxpayers.

It seems inconceivable that rights will be extended without some relation to duties. Contributory-based Social Security helps teach 'Citizenship'.

**Lord Oakeshott** concentrated on ways in which any system – contributory or universal- could be removed from political interference. Any improvement in the state pension system will need to be paid for, but it is politically difficult to publicly discuss ways of paying for reform, such as raising the state pension age.

One way to overcome this would be to appoint a state pension age commission, tasked solely with recommending future state pension ages, for example against a target of achieving an expected length of state pension payment of 25 years for people retiring in 25 years time.

This could have, say 9 members, one appointed by each of the main political parties, the Government Actuary and 5 independent appointments, with the majority being women. This could provide a stable background for the consideration of state pension policy.

A residency-based pension is the only way to help many people get a fair deal from the system, and is safer, clearer and more reliable than the existing system.

**Sally West** (Policy Manager, Age Concern) said that Age Concern wanted to see an improvement in the position of women pensioners, but that they were more concerned with the outcome of pension systems rather than the specific design. While recent work has concentrated on short-term measures to improve women's incomes, there were opportunities for more radical long-term reform.

One aspect used to differentiate contributory and universal pensions is the length of qualification periods, but that can vary under either system: it is possible to have a residency criteria of 40 years or a contribution record covering only 20 years.

There are gaps in the current system around those with complicated lives perhaps involving part-time work and caring for less than 35 hours, and it may not be possible to include all of these in a reformed contributory system which gives a strong case for a residency-based pension. But the strength of this case depends on how long people stay in these complicated situations - if it is only a short period a reduced contributory qualification period may have a similar impact to a residency-based pension.

The notion of fairness is very important in this debate. Many callers to Age Concern are concerned with the unfairness of the pension system in their particular case. But the ways in which it could be made fairer for them may make it less fair for others.

**The following points could be drawn from the discussion:**

- Improvements of women's state pension income is central to pension reform
- Improving the contributory system through increasing the number of activities qualifying for contributions would increase significantly administrative complexity without removing all of the gaps
- There is no agreement as to whether a contributory or residency-based pension would better protect pensions from political interference
- Fairness can take on more than one meaning in the context of this debate. Should everyone get the same, or should pensions reward those who contribute?
- Much is assumed about what the public thinks is 'fair', and public support is cited in support of both contributory and residency-based pensions. Further research into public perceptions of fairness would be helpful.

A show of hands at the end of the seminar showed:

- No support for making no change to the current system
- 6 votes in favour of modernising the existing contributory system
- 9 votes in favour of moving to a residency based system
- 4 votes not decided.

**Further points raised in discussion included;**

1. The real distinction is between a contributory and a residency-based pension. Either could be considered to be more 'universal' than the other, depending on the eligibility criteria, and a 'Citizen's Pension' could mislead, implying citizenship rather than residency.
2. It is important to consider the different costs of reform as part of any move away from the current system. Changing from the current contributory system to a universal system may cost less than £5bn per year extra by 2040 – not an insubstantial sum, but small relative to the Pension Credit by that time.
3. It may be easier to build consensus around the level of state pension than around a switch to a residency-based criterion, and to implement a single change rather than radical reform.
4. Modernisation of the current system may at least in part be able to be retrospective, and pensions for women reaching state pension age in future is likely to improve under the current system as the introduction of credits and HRP begin to take full effect (although gaps will still remain).
5. Tweaking the existing system may increase coverage of the contributory system, but will never cover all carers. To do so would require a very long audit trail covering things currently outside of the National Insurance system, such as a number of low paid jobs and/or caring for parents, neighbours and grandchildren.
6. Most women already expect to receive a full basic state pension and are indignant when they do not.
7. Child Benefit and Pension Credit already work on a residency-based qualification rather than contributory. Those who people believe are rightly excluded from the contributory system can still receive state support through Pension Credit.

8. The current combination of gaps in the contributory system and Pension Credit is undermining incentives to save, particularly for women. There needs to be an idea of 'you get something for doing something' to help rebuild a savings culture.
9. It is important to consider what people do after state pension age, and in particular the way that they can contribute to society, as well as considering what people did when they were of working age. A pension given as of right rewards participation better than one that is means-tested.
10. The current state pensions system is contributory, but 'entitlement' to the National Health Service is based on residency.
11. Pensions cannot be used to solve all of society's problems. Whether a pension is contributory or residence-based will not reduce the number of people who may be judged by some to be 'feckless' or lacking in self responsibility
12. It is important that any residency-based system is consistent with the treatment of pensions in the EU, especially around migrant workers and payment after state pension age. It is already possible for working tax credits to be paid to EU workers in the UK even if their families live elsewhere in the EU.
13. Although the residency-based pensions in New Zealand and Denmark have a lower benefit for a married person than a single person, they still operate on an individual basis (married women receive the same pension as married men). This is not an integral part of a residency-based pension. Options studied for the UK assume no difference in treatment. In New Zealand a major taskforce report acknowledged there is little rationale for different rates based on marital status alone.
14. New Zealand has a younger population than the UK, but faces similar challenges in terms of an increasing proportion of the population over age 65. New Zealand has better border controls than the UK, but still has high levels of multiculturalism and immigration.