

## A Stocktake on State Pension Reform


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## State Pension Reform – a trade union perspective



***Michelle Lewis***  
***TUC***



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## Summary


- What's wrong with state system?
- How do we improve it?




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## What's wrong with the state pension system?

- Inadequate
- Based on outdated principles
- Complex
- Reliance on means testing
- Trust







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## How do we improve it?

- Status quo
- increase basic state pension
- Re-index to earnings
- Further role of S2P
- Reduce means testing
- Increase over-80's payment
- impact of Pensions Credit


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## How do we improve it(2)?

- Women and pensions
  - Abolish 25% rule
  - Allow backdating NI contributions beyond current 6 yr limit
  - Further role of S2P
- Other options for reform

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## Priorities for TUC

- Improve retirement incomes of poorest pensioners
- Reaffirm state pension as foundation stone
- Address issue of women and pensions



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**PPI Seminar  
“A Stocktake on State Pension Reform”**

**Some Relevant Points From the First Report  
of the Pensions Commission**

Trevor Huddleston  
Head of Pensions Commission Secretariat &  
Analytical Team

## Three Themes

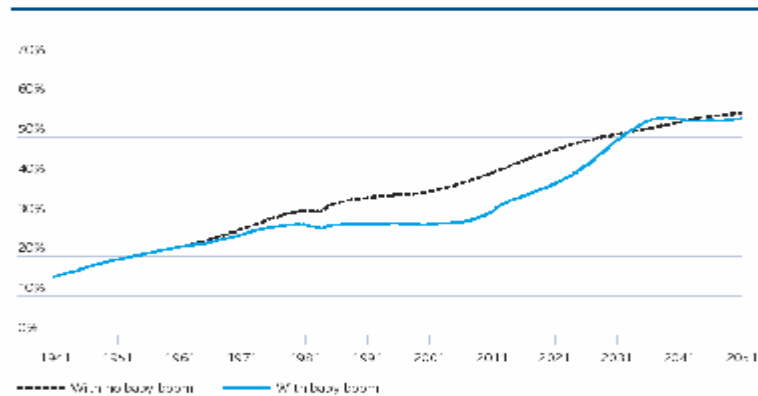
- The demographic context and the framing of policy questions.
- The four choices – No single answer.
- Some Implications of Current Complexity

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## The Policy Challenge

**Figure E.8** Impact of the 1940s-1960s Baby Boom on the Old-age Dependency Ratio



Source: Pensions Commission's analysis based on a synthetic model of the England and Wales population

## Three Themes

- The demographic context and the framing of policy questions.
- The four choices – No single answer.
- The Implications of Current Complexity

## Looking forward to 2050, The Pensions Commission Report Identified 4 Options

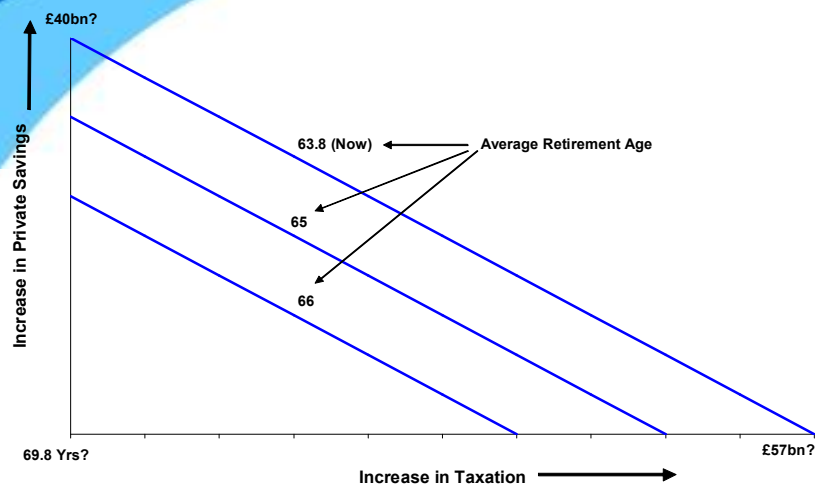
1. Future pensioners will on average be poorer relative to average net incomes than today; or
2. Taxes/NI contributions will have to rise to pay for pensions or other public spending be cut to make room for pensions; or
3. Each generation will have to save more, and will be reliant on the next generation also choosing to save more and therefore buying the larger stock of assets accumulated by the prior generation; or
4. Average retirement ages will have to rise

## No Single Option Looks Attractive

“The Commission’s current judgement is that Option 1 is unattractive in respect to the vast majority of pensioners, while a **sole** reliance on one of Options 2, 3 or 4 is unlikely to be feasible”.

“We therefore believe that the best policy for society to choose, and the one which is likely to reflect well-informed individual preferences, would involve some mix of Options 2, 3, and 4. A survey by the Association of British Insurers (ABI) suggests that when people are forced to choose between the four options, very few people favour a fall in pensioners’ relative living standards, and the two most favoured responses are an increase in the average retirement age and a higher rate of saving”.

### How to Think About the Trade-Offs Between Higher Taxes, More Private Saving and Later Average Retirement Ages



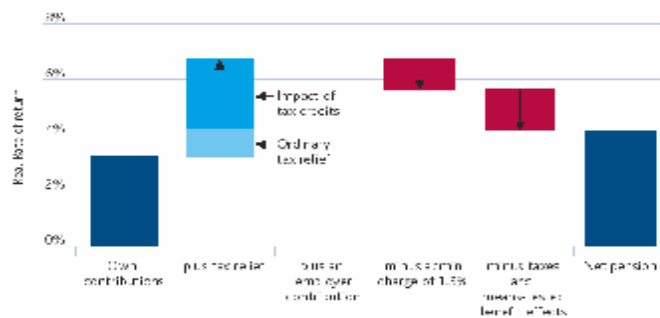


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## The Current System is Complicated.

- **Figure C.28** Effective Real Rate of Return for Stylised Individual who pays Basic Rate Tax and is on Working Tax Credit in Working Life and is on Means-tested Benefits in Retirement.



Source: Pensions Commission analysis.

Note: The rate of return of individual, being across both accumulation and decumulation is 3.18%. We assume that he does not get a 1% and does not get a 1% contribution to his pension. He pays an annual management charge of 1.5%.

**Complexity of the State System:  
The Impact on individuals and other players**

- Can individuals make appropriate and well informed decisions?
- Will IFA's give any advice to people who might be in receipt of income related benefits in retirement?
- Will firms be willing to provide advice; is automatic enrolment a good policy or will firms be wary?

**Complexity of the State System:  
The Challenge for Reformers**

- People receiving pensions in the early part of the 21<sup>st</sup> century will have accrued rights to Graduated Retirement Benefit, SERPS under the original formula; SERPS under the formula as revised in 1986 and S2P.
- Policy makers must consider how these existing accruals would be dovetailed into any new arrangements. Transitional protection; buy-outs; etc.
- Fundamentally: how do we get from here to there?

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## State Pension Reform

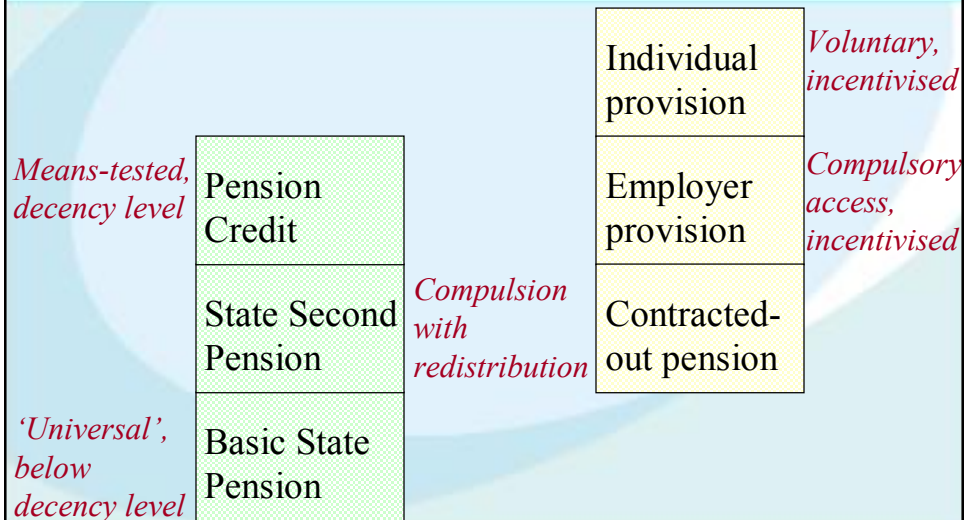
Ian Naismith

*Head of  
Pensions Market Development*



PPI Seminar  
25 November 2004

## The current system



## Issue 1: Primary & secondary state pensions

- Increase the basic pension to decency level
  - Simple
  - Minimises means-testing
  - Fair to carers etc
- Continue a two-tier system
  - Some link between pre and post-retirement income
  - S2P benefits low earners
  - Fair to 'workers'
  - Need to do something for self-employed

## Issue 2: Contracting-out

- Many positive features...
  - Pre-funded by government
  - Encourages private provision
  - Profitable for providers - subsidises other business
- ...but considerable difficulties
  - A no-win situation for advice at present
  - Would government give generous earnings-related rebates with flat-rate S2P?

An acceptable price for resolving other issues?

## Issue 3: Means-testing

- Pensions Credit - a short-term expedient?
  - Some credit is better than none!
  - But at its current level it's a disincentive
- Is sensible reform an option?
  - Reduce deduction from 40% to 30% for break-even
  - Reduce to 22% to give incentive

Is widespread means-testing socially undesirable?

## Conclusions

- No perfect solution
- Broad agreement on principles - debate tends to be about priorities
- Important to look at whole picture, not just individual components
- Sorting state pensions would largely resolve the compulsion issue

## Important notes

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## The Case for Change

Mervyn Kohler  
Head of Public Affairs



**Help the Aged**

## The Case for Change

If the average pensioner is likely to qualify

Mass means-testing is an imperfect (inefficient)



## Changing the Level

Pitched to avoid poverty

- Shopping basket?
- Linked to 60% mean household income?

Incentivise additional pension saving





## Changing the Age

65 feels right

Chattering classes don't understand the burn-out factor

Incentivise deferment – open more opportunities to work

Economic consequences not devastating



## Changing the Index

Anything but prices



## Changing the Eligibility

Veering towards citizenship basis

Problem: household vs. individual entitlement



## Changing the S2P

No longer a SERPS, just a top-up

Unnecessary if other State Pension changes implemented



## Changing the World of Work

Retraining opportunities

Mentoring

Organisation of time



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**PPI**

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