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A reference manual by the Pensions Policy Institute

This version of a guide to the UK pensions system reflects the current position of, and legislated future changes to, the UK pension system as at May 2019. Any change in Government policy that may have occurred after that date is not included in this version.

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AN INTRODUCTION TO THE UK PENSIONS SYSTEM

The foundations of the UK pension system were laid in the 1940s. Since the 1960s, successive Governments have made many changes to both state and private pensions resulting in today's pension system, which is complex and multi-layered.

This document provides a description of the UK pensions system for the purposes of considering pensions policy. It should not be used as a basis for making individual financial decisions.

This guide reflects the current position of the UK pensions system as at 1 May 2019. Any changes in Government policy that have occurred after that date are not included in this version.

The Pensions Primer is aimed at a wide audience. For this reason, sections vary in complexity. The initial guide gives an outline of the UK Pensions System and the influences of current policy. There are signposts throughout the Primer to the Appendix, which provides additional, more detailed explanations of past and present policies.

To explain the UK pensions system, this report uses a multi-tier framework. The UK pension system possesses three tiers:

- **Tier 1** is provided by the state and consists of a basic level of pension to which almost everyone either contributes or has access, providing a minimum level of retirement income.
- **Tier 2** is also administered by the state and aims to provide pension income that is more closely related to employees’ earnings levels. Tier 2 is less redistributive (from higher-income to lower income) than Tier 1. Tier 1 and Tier 2 operate on an unfunded ‘pay-as-you-go’ contributory basis, through the National Insurance (NI) system, though people can no longer accrue entitlement to Tier 2.
- **Tier 3** is voluntary (private) pension arrangements that are not directly funded by the state. Private pension contributions, from the employer and/or the individual, fund designated pensions for the individual. The primary aim of private pensions is to redistribute income across an individual's lifetime, and not to redistribute income from higher-income to lower-income people. Tier 3 includes pensions arising from automatic enrolment, a policy requiring employers to enrol eligible employees into a qualifying workplace pension scheme.

Chart 1 illustrates the three tier UK pensions system as it stands today. Although means-tested benefits span across the three tiers, they are covered in the First tier provision section. With the introduction of the "single tier" new State Pension, these 3 tiers will eventually become a two tier system with a “state” tier and a “private” tier.
# THE CURRENT UK PENSION SYSTEM

Chart 1

## TIER 1: STATE PENSION

**PUBLIC**
Unfunded – pay as you go system that is paid through National Insurance contributions

Redistributes money throughout the population to provide all individuals with a minimum standard of living

basic State Pension, new State Pension

## TIER 2: ADDITIONAL STATE PENSION

**PUBLIC**
This provides individuals with additional state pension more closely related to their earnings level than the flat rate that people receive from the first tier

With the new State Pension, from April 2016 people are no longer able to accrue entitlement to the additional State Pension or Savings Credit

Graduated Retirement Benefit (GRB), State Earnings Related Pension Scheme (SERPS), State Second Pension (S2P)

## TIER 3: PRIVATE PENSION

**PRIVATE**
Funded through individual and/ or employer contributions

Contributions and returns receive tax relief

Intended to distribute earnings across the life course

DB and DC Pensions

Occupational/ Personal/Multi-Employer Schemes

---

**PUBLIC**
Means-tested

Pension Credit = Guarantee Credit + Savings Credit

Public Tier benefit = Housing Benefit

Universal benefits = Winter fuel allowance
FIRST TIER PROVISION

The first tier is provided by the State and consists of a basic level of pension provision to which everyone either contributes or has access, providing a minimum level of retirement income. Included in this section are:

- The basic State Pension (bSP) and additional State Pension
- The new State Pension
- Means-tested benefits

The first tier operates on a ‘pay-as-you-go’ basis, through National Insurance (NI) and general taxation. NI contributions, levied on workers’ earnings, are used to pay the basic State Pension/new State Pension. Pension Credit is funded through general taxation.

THE NEW STATE PENSION (nSP) - FOR PEOPLE REACHING STATE PENSION AGE ON OR AFTER 6TH APRIL 2016

The new State Pension (nSP), introduced in April 2016, is a contributory pension in the sense that the final amount of nSP paid to an individual depends on the number of National Insurance contributions (NICs) made (or credited) before reaching State Pension age (SPa). The nSP replaced the basic State Pension and additional State Pension in order to make the State Pension more streamlined, easier to understand, and to provide a more comprehensive basic level of income to pensioners above the level of means-tested benefits.

The nSP is designed to redistribute wealth across the population to provide all individuals with a minimum standard of living and to provide a base for saving into a private pension. It is a flat rate pension payable once an individual reaches SPa. Subject to having made the same number of contributions, individuals will receive the same level of benefit, irrespective of the size of their contributions. An individual pensioner with a complete NI contribution record of 35 years or more is eligible at their SPa to receive the full nSP of £168.60 a week (2019/20), although those who have contracted out may receive a reduced amount.

QUALIFYING YEARS AND NATIONAL INSURANCE CONTRIBUTIONS

State Pension entitlement is based on an individual’s NI contribution record. Any tax year in which an individual makes, or is credited with making, sufficient NI contributions is known as a qualifying year.

There are 27 activities that can credit someone into the State Pension without their having to pay contributions. Credit will be given if, for instance, an individual is entitled to Statutory Sick Pay or Statutory Maternity, Paternity or Adoption Pay, Jobseekers Allowance, Employment and Support Allowance, Carer’s Allowance²

NI contribution rules are complex; there are a number of ways in which contributions can be made or credited. For example, individuals who are self-employed pay a different level than individuals who are employed, and people can make voluntary contributions to fill gaps in their contribution record.

2. www.gov.uk/national-insurance-credits/eligibility
For people reaching SPa on or after 6th April 2016, 35 years of National Insurance contributions are necessary to qualify for a full new State Pension. A minimum of 10 qualifying years are necessary to get any new State Pension.

Please refer to Appendix 1 for more information on NI, what constitutes as a qualifying year and the different classes of NICs contributions.

STARTING AMOUNT (FOUNDATION AMOUNT)
When calculating the amount received under the nSP, a “starting” amount will be calculated for each individual, based on their entitlement built up under the state pension system prior to 6th April 2016. This amount will be compared to the amount that the individual would have built up in the nSP system had it been in place. Individuals will then take forward the higher of the two amounts (adjusted for time spent contracted-out of the additional State Pension) into the new system.

If the starting amount is higher than the nSP level, the amount above the nSP level will be paid on top of the nSP. This amount is called a “protected payment” and increases each year with the Consumer Prices Index (CPI).

If the starting amount is less than the nSP level, each qualifying year accrued after April 2016 will be added on top of the starting amount until reaching SPa or reaching the full nSP amount. Each year adds £4.82 a week to retirement income (£168.60 divided by 35, 2019/20).

CONTRACTING-OUT
The new State Pension (nSP) replaces the basic State Pension (bSP) and the additional State Pension (Click to see Tier 2). Between 1978 and 2016, it was possible to contract out of the additional State Pension. Where employees were contracted-out, both employees and their employers paid lower NICs contributions (through a rebate) on the condition that the pension scheme provided pensions broadly in line with, or better than, the future state benefits that the individual was giving up by contracting-out. In 2015/16, this meant that contracted-out employees paid NICs contributions at a rate of 10.6% instead of 12%, and their employers paid NICs contributions at a rate of 10.4% instead of 13.8% up to the Upper Accrual Point (UAP) of £40,040. In turn, employees who were contracted-out did not accrue entitlement to SERPS or S2P (additional State Pension) during those years.

Under the nSP, people who contracted-out of SERPS and/or S2P are treated as having built up less State Pension rights than similar individuals who did not contract out. Part of the ‘state’ pension, for those who contracted-out will be delivered through a private pension scheme, so an equivalent value is deducted from their ‘foundation’ amount at the time the nSP is introduced. This means that an individual who has been contracted-out will have a lower foundation amount than an identical individual who has not been contracted-out.

People who contracted-out and reached SPa on or after 6th April 2016 can receive an estimate of the additional State Pension they would have built up if they did not contract out. This is known as the contracted-out pension equivalent (COPE).

If people who contracted out are close to retirement then they are likely to receive a lower nSP than an individual who has not contracted-out. However, if these people have a number of years still to go to SPa, then the contracted-out individual may receive a similar or equivalent nSP at SPa to the individual who has not contracted-out, as long as they continue to add further qualifying years to their National Insurance Record.

https://www.gov.uk/new-state-pension/how-its-calculated
**CASE STUDIES:**

Robert is a median earning male who has never been contracted-out. At age 45 in 2016 his foundation amount is £127 a week. This is made up from £87 of basic State Pension (bSP) entitlement, and £40 of SERPS/S2P (from his 22 qualifying years). When he retires at 67 in 2038, he will have had additional qualifying years and as he will have exceeded the required 35 years will receive the full nSP (£168.60 a week in 2019/20), which replaces his basic and additional State Pension.

Graham is a median earning male who has been contracted-out for his entire career prior to 2016. At age 45, his foundation amount is £87 a week from basic State Pension entitlement (from his 22 qualifying years). As he had contracted-out of the additional bSP, he has not accrued the additional entitlement and paid less NIcs contributions. When he retires at 67 in 2038, he receives the full nSP amount (£168.60 a week in 2018/19) as he will have exceeded the required 35 years and has enough qualifying years on top to overcome his contracted-out deduction. He also receives the contracted-out private pension equivalent of £40 in 2016 earnings terms.

Sharon is a median earning woman who has been contracted-out for her entire career prior to 2016. At age 60 in 2016, her foundation amount is £119.30 a week. Her foundation amount is the higher of her entitlement under the old State pension system of £119.30 a week from bSP entitlement (from having a full qualifying years already), compared to a new State Pension (nSP) entitlement of £105.65 (£155.65 full nSP minus a £50 Contracted-out deduction). When she retires at 66 in 2022, she receives her foundation amount plus she has been able to accrue 6 further qualifying years on top, bringing her total pension, in 2019/20 terms to £158.10 (129.20 revalued foundation amount plus 6/35 x 168.60). She also receives the contracted-out private pension equivalent of £50 in 2016 earnings terms.

**STATE PENSION AGE (SPA)**

The State Pension age (SPA) is the minimum legal age at which a State Pension can be claimed. SPA depends on an individual’s birth date.

SPAs for both men and women is currently increasing incrementally from age 65 to age 66 in a staged process until October 2020 (Pensions Act 2011). Refer to Appendix 2 for a table on SPAs increases.

Under previous legislation, SPA was scheduled to increase to age 67 between 2034 and 2036 and to age 68 between 2044 and 2046. However, the Government has brought forward the rise to age 67 to now take place between 2026 and 2028. This change was included in the Pensions Act 2014.

**BRINGING FORWARD THE SPA RISE TO 68 AND THE MECHANISM FOR DETERMINING FUTURE RISES**

The Pensions Act 2014 sets out the Government’s plans for the SPAs in the future (Chart 2). This includes a review of the SPAs at least once every 5 years, the review to be based around the principle that people should expect to spend a third or less of their adult life in retirement (based on analysis provided by the Government Actuary’s Department and an independently led body). For this purpose, adult life is defined as starting at age 20. In the Autumn Statement 2013, the Chancellor suggested this might result in the SPA increasing to age 68 by the mid-2030s and to 69 by the late 2040s.

In March 2017, the final report of the Independent State Pension Age Review was published. The report recommended that the SPAs should increase to age 68 over a two-year period starting in 2037 and ending in 2039, to reflect changes in life expectancy. The report also recommended that SPAs should not increase more than one year in any ten-year period, unless there are exceptional changes to the underlying data (e.g., costs or life expectancy projections). The Government is unlikely to legislate for future SPAs changes until another independent review is conducted during the next Parliament.

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5 Announced in the Chancellor’s Autumn Statement, 2013: www.gov.uk/government/topical-events/autumn-statement-2013
7 DWP (2013) The core principle underpinning future State Pension age rises: DWP background note
8 HM Treasury (2013) Autumn Statement
DEFERRING NEW STATE PENSION

Individuals can choose to defer the commencement of their nSP after reaching SPa in return for an increase in the level of State Pension payments, also known as an enhanced pension.

For each 9 weeks of deferral, people can receive an increase of 1% in their pension. This is an equivalent of around 5.8% for each year people defer. After claiming, the extra amount will increase in line with growth in the Consumer Prices Index (CPI).

CASE STUDY:
At Lauren’s SPa in May 2018 she has 35 qualifying years, so would have been entitled to receive a full nSP of £164.35 a week.

She decides to defer receiving her nSP for a year until May 2019. At that time, when she chooses to start receiving her pension, the rate of nSP is £168.60 a week. Lauren is entitled to receive the full current rate of nSP plus an enhancement resulting from the deferment of £9.74 a week (£168.60 x 1% x 52 weeks/9).

Lauren’s total state pension in 2019 is £173.85 (£168.60 + £9.74).

https://www.gov.uk/deferring-state-pension/what-you-get
Between 1974 and 1979, the State Pension increased annually by the greater of the increase in National Average Earnings (NAE) or the increase in the Retail Prices Index (RPI) (Chart 3). Since 1979, annual increases have generally been linked to RPI. The net effect of past uprating has been that, although the value of the full bSP has increased in price terms since the 1970s, it has reduced relatively to average earnings from 24% of NAE in 1974 to an estimated 16% of NAE in 2009. Before 1974, uprated on an ad-hoc basis. From 2001 to 2011, uprated by the greater the increase between National average Earnings and the Retail Price Index. From April 2011, the higher of 2.5%, the increase in earnings, or CPI, ‘Triple Lock’. However, legislation only provides that the increase in the State Pension must be at least at the rate of the increase in the general level of earnings, therefore the bSP or nSP may be re-indexed at some point in the future, unless the triple lock becomes enshrined in legislation.

Between 2001 and April 2011, the State Pension was increased by the greater of 2.5% or the RPI. The net effect is that, although the value of the State Pension increased in price terms, when compared to National Average Earnings (NAE) its value has gradually eroded since 1979 (Table 1). The new State Pension introduced in April 2016 provides 24.2% of NAE, improving the value relative to earnings in comparison to the bSP, (though full entitlement to bSP and additional State Pension is often above 24.2% of NAE). From 2001 to 2011, Uprated on an ad-hoc basis. From April 2011, the higher of 2.5%, the increase in earnings, or CPI, ‘Triple Lock’.

13 webarchive.nationalarchives.gov.uk/20130129110402; www.hm-treasury.gov.uk/fin_consumer_finprovision.htm
The Government has committed to maintaining the triple lock until 2022.

**TABLE 1: UPRATING OF BSP AND NSP IN RELATION TO NATIONAL AVERAGE EARNINGS**

<table>
<thead>
<tr>
<th>Date</th>
<th>Weekly Amount</th>
<th>Adjusted to April 2019</th>
<th>Weekly National Average Earnings</th>
<th>As a percentage of NAE</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>bSP</td>
<td>nSP</td>
<td>bSP</td>
<td>nSP</td>
</tr>
<tr>
<td>Oct 1972</td>
<td>£6.75</td>
<td>£87.47</td>
<td>£32.00</td>
<td>21.1%</td>
</tr>
<tr>
<td>Jul 1974</td>
<td>£10.00</td>
<td>£103.90</td>
<td>£41.70</td>
<td>24.0%</td>
</tr>
<tr>
<td>Nov 1977</td>
<td>£17.50</td>
<td>£106.44</td>
<td>£70.20</td>
<td>24.9%</td>
</tr>
<tr>
<td>Nov 1979</td>
<td>£23.30</td>
<td>£111.74</td>
<td>£89.60</td>
<td>26.0%</td>
</tr>
<tr>
<td>Nov 1982</td>
<td>£32.85</td>
<td>£114.82</td>
<td>£136.50</td>
<td>24.1%</td>
</tr>
<tr>
<td>Apr 1987</td>
<td>£39.50</td>
<td>£112.11</td>
<td>£198.90</td>
<td>19.9%</td>
</tr>
<tr>
<td>Apr 1992</td>
<td>£54.15</td>
<td>£112.72</td>
<td>£304.60</td>
<td>17.8%</td>
</tr>
<tr>
<td>Apr 2010</td>
<td>£97.65</td>
<td>£126.63</td>
<td>£598.30</td>
<td>16.3%</td>
</tr>
<tr>
<td>Apr 2011</td>
<td>£102.15</td>
<td>£125.91</td>
<td>£602.60</td>
<td>17.0%</td>
</tr>
<tr>
<td>Apr 2012</td>
<td>£107.45</td>
<td>£128.02</td>
<td>£607.80</td>
<td>17.7%</td>
</tr>
<tr>
<td>Apr 2013</td>
<td>£110.15</td>
<td>£127.56</td>
<td>£620.20</td>
<td>17.8%</td>
</tr>
<tr>
<td>Apr 2014</td>
<td>£113.10</td>
<td>£127.80</td>
<td>£620.80</td>
<td>18.2%</td>
</tr>
<tr>
<td>Apr 2015</td>
<td>£115.95</td>
<td>£129.85</td>
<td>£627.00</td>
<td>18.5%</td>
</tr>
<tr>
<td>Apr 2016</td>
<td>£119.30</td>
<td>£131.86</td>
<td>£172.04</td>
<td>£644.90</td>
</tr>
<tr>
<td>Apr 2017</td>
<td>£122.30</td>
<td>£130.58</td>
<td>£170.36</td>
<td>£661.10</td>
</tr>
<tr>
<td>Apr 2018</td>
<td>£125.95</td>
<td>£164.35</td>
<td>£169.77</td>
<td>£685.30</td>
</tr>
<tr>
<td>Apr 2019</td>
<td>£129.20</td>
<td>£168.60</td>
<td>£168.60</td>
<td>£701.06</td>
</tr>
</tbody>
</table>

Refer to Appendix 3 for a more detailed table on the historic upratings, and for the projected level of bSP and nSP compared to average earnings.
THE BASIC STATE PENSION (BSP) – FOR PEOPLE REACHING STATE PENSION AGE BEFORE 6TH APRIL 2016

There are various changes between the basic State Pension (bSP) and the new State Pension (nSP). Table 2 provides a comparison of the State Pension systems before and after 6th April 2016.

<table>
<thead>
<tr>
<th></th>
<th>Basic State Pension (for those reaching SPa before 6th April 2016)</th>
<th>New State Pension (For those reaching SPa on or after 6th April 2016)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Full amount</strong></td>
<td>The full amount of bSP is £129.20 a week (2019/20 rate).</td>
<td>The full amount of the nSP is £168.60 a week (2019/20 rate).</td>
</tr>
<tr>
<td><strong>Qualifying years</strong></td>
<td>People retiring between 6 April 2010 and 5 April 2016 needed 30 qualifying years to receive a full bSP. There was no minimum amount of qualifying years required from 2010.</td>
<td>Need 35 years of National Insurance contributions or credits to receive a full rate of pension. People will also need a minimum of 10 qualifying years to qualify for any State Pension.</td>
</tr>
<tr>
<td><strong>Pension Credit</strong></td>
<td>People reaching SPa before April 2016 were eligible to receive Guarantee Credit and Savings Credit if they met certain criteria.</td>
<td><strong>Savings Credit is unavailable</strong> to people who reach SPa on or after 6th April 2016. Means-tested support will continue to be available through the Guarantee Credit element of Pension Credit. For a transitional period of 5 years (until April 2021), support will be retained for those people who may have been eligible for Savings Credit under the old system.</td>
</tr>
<tr>
<td><strong>Additional State Pension and contracting-out</strong></td>
<td>Prior to April 2016, members of some pension schemes could contract out of the additional State Pension and pay less in National Insurance contributions.</td>
<td>Under the nSP, further entitlements to the additional State Pension (Tier 2) have been abolished. Schemes are no longer able to contract out, meaning National Insurance contributions may increase for those who were contracted-out prior to April 2016.</td>
</tr>
</tbody>
</table>
**Deferral**

Before April 2016, individuals could defer BSP and receive either an enhanced pension or a taxable lump sum. For each **5 weeks** of deferral, people could receive an increase of 1% in their pension. This was an equivalent of 10.4% for each year people deferred.

From April 2016, individuals who defer can only receive an enhanced pension. For each **9 weeks** of deferral, people can receive an increase of 1% in the pension. This is an equivalent of just under 5.8% for each year people defer.

**Uprating**

BSP will continue to be uprated by the **triple lock** for 2019/20. The additional State Pension is uprated by the Consumer Prices Index (CPI).

nSP will continue to be uprated by the **triple lock** for 2019/20. The protected payment is uprated by the Consumer Prices Index (CPI).

**State Pension based on partners contribution**

Before April 2016, some people received a State Pension based on their partner’s National Insurance contributions. These included individuals who were expecting to receive a pension based on their spouse or civil partner’s National Insurance contributions and married women who paid reduced rates of National Insurance on the assumption that they would receive a derived pension based on their husband’s contributions.

For more details on the categories of BSP, please refer to Appendix 4.

The National Insurance record of an individual’s spouse or civil partner will only be relevant up to and including the tax year 2015/16 to calculate any entitlement.

Under the measures set out in the Pensions Act 2014 those who reach SPa under the new State Pension will not be able to claim derived entitlement based on their partner’s State Pension entitlement. However, women who paid reduced rates of National Insurance contributions at any point during the 35 years before their SPa will be able to claim an amount equivalent to the full rate of the ‘married woman’s’ basic pension rate.
MEANS-TESTED BENEFITS

In addition to the State Pension, there are several means-tested benefits that pensioners may be eligible for, depending on their circumstances.

Pension Credit (PC) has two components:

- **Guarantee Credit (GC).** It is currently payable from age 65 ¼, rising to age 66 by October 2020. The minimum age for receiving Guarantee Credit is increasing in line with increases in SPa (as introduced by the Pensions Act 1995). This means the Guarantee Credit qualifying age is gradually increasing to 66 by October 2020.

- **Savings Credit (SC).** Savings Credit is no longer available for people retiring after 6th April 2016, but is still paid to those already in receipt.

GUARANTEE CREDIT

Guarantee Credit is the main means-tested benefit currently paid to those aged 65 ¼ and above (rising to age 66 by October 2020). People (or households) become eligible for Guarantee Credit if other sources of income do not reach a certain level. If claimed, Guarantee Credit provides a safety net of a minimum level of income. Its effect is redistributive – the benefit is paid from taxes that are related to income and only paid to those on low income.

In 2019/20, Guarantee Credit provides a minimum income of £167.25 a week for single people and £255.25 a week for couples. Guarantee Credit entitlement can be higher for disabled people, people with caring responsibilities or people with a mortgage.

The Pensions Act 2007 requires the Guarantee Credit to be increased by a percentage at least equal to the increase in the general level of earnings. For 2019/20, the Government increased the Guarantee Credit by 2.6% in line with the cash increase in the nSP, and slightly above the increase in earnings.

SAVINGS CREDIT

With the introduction of the nSP and the removal of the mechanism for accruing entitlement to additional State Pension, Savings Credit is no longer available for people reaching SPa after 6th April 2016. Savings Credit was designed to ensure that those who made some private provision for retirement, or had entitlement in excess of the State Pension, including State Earnings Related Pension Scheme (SERPS) and State Second Pension (S2P), were better off than those who had made no provision.

The maximum amount payable under Savings Credit is £13.72 a week for a single person and £15.35 a week for a couple from April 2018 for those already in receipt. For every £1 of income received above the level of the Savings Credit threshold (£144.38 for single pensioners and £229.67 for couples, in 2019/20), but below the level of Guarantee Credit, Savings Credit pays an additional benefit of 60p. The credit is then ‘tapered down’ for additional income above the Guarantee Credit level.

CASE STUDY:

Eve retired under the old State Pension system. She is entitled to a bSP of £120.59 a week (from her 28 qualifying years), which is £8.61 below the maximum entitlement for a single person. She also receives an occupational pension of £30.00 a week giving her a total weekly income of £150.59.

She is entitled to a guaranteed element of Pension Credit of £16.66 (to increase her income to the Guarantee Credit level of £167.25 a week). She also receives Savings Credit of £3.72 a week. This is worked out as it is 60% of her weekly income above the Savings Credit threshold of £144.38, giving her a total weekly income of £170.97.

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17 The State Pension Credit Act 2002 sets the qualifying age for the Guarantee Credit to be the same as the State Pension age for women.
18 PC10S – A detailed guide to Pension Credit for advisers and others (April 2015)
20 From ongoing employment, SERPS, Graduated Retirement Benefit, occupational schemes, personal pensions and assumed income from capital savings
21 Department for Work and Pensions (DWP) 2018 Proposed benefit and pension rates 2019 to 2020
On January 14, 2019, the Government announced that it would be implementing a section of the Welfare Reform Act 2012, making changes to the age at which some people could claim Pension Credit.

Before May 15, 2019, people in mixed-age couples (where one person is above SPa and one below) were able to claim Pension Credit based on the age of the older person. After this date, claims can only be made based on the age of the younger person. People who qualify before this date can make a backdated claim until August 13 2019.

As well as mixed-age couples where one reaches or has already reached SPa, the following will also be unable to claim Pension Credit.

- Single pensioners who start living with a partner who has not reached the qualifying age on or after 15 May 2019.
- People whose circumstances change and become entitled again at any time on or after 15 May, but their partner has not reached the qualifying age.

The Government defines a partner as “a person you live with as if you were a married couple”, regardless of whether or not they are married or in a civil partnership.

It is expected that people in mixed age couples who would have claimed Pension Credit will have instead to claim Universal Credit, or that existing claims for Universal Credit will continue until the younger partner reaches SPa.

**UNIVERSAL CREDIT**

Universal Credit (UC) is the new benefit for working age people, and is intended to bring a number of legacy benefits into one system. These are:

- Child Tax Credit
- Housing Benefit
- Income Support
- Income-based Jobseeker’s Allowance (JSA)
- Income-related Employment and Support Allowance (ESA)
- Working Tax Credit

It is designed specifically for people who are out of work or who are on a low income, and was explicitly created to encourage claimants to take up and/or increase paid work. To this end, its unique feature is that for every pound earned while working and claiming UC, the claimant can keep 37p up until the point that their allocated amount is met or exceeded. The allocated amount (maximum UC rate) for a couple is currently £114.85 per week.

To read about these benefits in more detail, please refer to Appendix 5.
OTHER FORMS OF MEANS-TESTED RETIREMENT INCOME

Housing Benefit (HB) and Council Tax Reduction are means-tested benefits available to both pensioners and people under State Pension age, though working-age people will receive support for housing costs from Universal Credit if they are new claimants. Although they are not part of the first tier of pension provision in the UK, they are included here because they are important benefits that make up a retirement income for many older people.

Housing Benefit is paid to people on low incomes who rent their home. There is no set amount a person may receive though there are caps on different household types. It is designed to help with housing costs, including rent and some accommodation-related service charges. It is paid to renters who claim the benefit once they have been assessed as being eligible.

Not everybody that is eligible claims HB. Official estimates show that, in 2016/17, 16% of around 1.8m pensioner households who were eligible did not take up their benefit. For a more detailed description of HB, please refer to Appendix 6.

Council Tax Reduction (CTR) is a rebate scheme to provide help with up to 100% of an individual’s Council Tax. Local councils design their own scheme.

According to official estimates, take-up of Council Tax Benefit (the precursor to Council Tax Reduction) was relatively low; in 2009/10 between 31% and 38% of pensioner households who were eligible did not take up their benefit. Since then, the provision of Council Tax Benefit has been devolved to individual Councils, and there is currently no more up to date data on levels of take-up. For a more detailed description of Council Tax Reduction, please refer to Appendix 7.

Pensioners receive other, non-pension benefits that could be considered as part of the first tier of provision:
- Benefits individually assessed for specific purposes for example, Attendance Allowance
- (Near) Universal benefits for all or most people at a certain age for example, free TV licenses and Winter Fuel Payments

Please refer to Appendix 8 to see a complete list of other non-pension benefits pensioners may receive.

SECOND TIER PROVISION

The first and second tier of pensions are both provided by the state, however they operate in different ways. The UK’s second tier of state pension provision operates on an unfunded ‘pay-as-you-go’ contributory basis, through the National Insurance (NI) system. Benefits are payable from State Pension age (SPa), but can be deferred. The self-employed were excluded from second tier provision prior to April 2016.

The original aim of the second tier was to provide further pension income to employees more closely related to their earnings level than the flat rate that people receive from the first tier. Though people can no longer build up entitlement to the second tier of the state pension, prior to April 2016, contributions were made in proportion to earnings (in a band between minimum and maximum limits). Benefits reflect these contributions, resulting in less redistribution across the population than in the first tier.

Second tier provision in the UK has existed in three different guises (Chart 4):

- Graduated Retirement Benefit (GRB: 1961 to 1975) – For more information, go the Historical Annex.
- State Earnings Related Pension Scheme (SERPS: 1978 to 2002) – For more information, go to Appendix 9.
- State Second Pension (S2P: from April 2002 to April 2016) – For more information, go to Appendix 10.

ADDITIONAL STATE PENSION HAS EXISTED IN 3 DIFFERENT GUISES

Chart 4

Graduated Retirement Benefit (GRB) was a compulsory scheme where employees paid graduated contributions. Between 1975 and 1978 there was no accrual of additional State Pension entitlement.

State Earnings Related Pension Scheme (SERPS). The original aim of SERPS was to provide a pension of 25% of band earnings, however subsequent changes to SERPS have reduced its value.

The State Second Pension (S2P) replaced SERPS. The S2P targets greater resources at the lower paid and is therefore more redistributive than SERPS.

From 2016, people can no longer build up entitlement for the additional State Pension.
HOW ADDITIONAL STATE PENSIONS WERE ACCRUED

Prior to abolition, the pattern of accruing benefits under S2P was based on two earnings bands and two accrual rates. For low earners, a flat rate of S2P pension was accrued. Higher earners accrued an additional earnings-related benefit alongside the flat rate accrual. Disabled people, and some individuals with caring responsibilities, could be credited into the flat rate part of S2P. For more information on S2P accrual, please refer to Appendix 11.

Contracting-out

Prior to 6th April 2016, NI contributions went towards the basic State Pension, and also towards the additional State Pension (Chart 5).

PRIOR TO APRIL 2016, PEOPLE COULD CONTRACT OUT OF THE ADDITIONAL STATE PENSION IF THEIR PRIVATE PENSION PROVIDED AN EQUIVALENT AMOUNT

As members of Defined Benefit schemes had accrued private pension provision, they could opt out of contributing to the additional State Pension. This means they paid lower NI contributions, but did not receive additional State Pension income from the state. Instead, their employer was responsible for providing an actuarially assessed equivalent value of private pension. This is known as contracting-out.

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25 Earnings between the Lower Earnings Limit and the Upper Accrual Point. Before 6 April 2010, there were three bands accruing benefits at 40% 10% and 20%. Following provisions in the Pensions Act 2007, the former second and third bands have been merged into a single band accruing benefits at 10%.
Prior to April 2012, members of Defined Contribution pension schemes were also able to contract out of S2P.

Defined Benefit pension schemes could choose for their members to forgo additional State Pension entitlement provided that the scheme promised to pay benefits that were at least as valuable as the additional State Pension benefits. Individuals who contracted-out paid lower NI contributions, and so did their employers, since they were considered to be contributing the equivalent amount into the private pension scheme. The reduction in the level of NI contributions was known as the ‘contracting-out’ rebate.

The size of the rebate was set every 5 years with advice from the Government Actuary Department, and acted as an incentive or disincentive to contract out depending on whether the return on the rebate was perceived to be of higher or lower value than the benefit payable under S2P.

For some additional elements associated with contracting-out, please refer to Appendix 12.

With the introduction of the new State Pension in April 2016, further accrual for the additional State Pension was abolished. People who had contracted-out now have to pay the full National Insurance contributions.

UPRATING OF ADDITIONAL STATE PENSION
The additional State Pension is uprated by the Consumer Prices Index (CPI). The annual increase in CPI was 2.4% in September 2018, therefore the additional State Pension increased in line with this in April 2019, with the maximum amount of additional State Pension increasing from £172.28 (2018) to £176.41 (2019).

The following gives a summary of the public pension system that has been discussed. This includes the new State Pension, the additional State Pension, and means-tested benefits. As the additional State Pension can no longer be accrued, it has been shaded out to reflect this change.

Contributory pension with a flat rate of £168.60 a week for individuals who have 35 qualifying years. People will also need a minimum of 10 qualifying years to qualify for any state pension.

Redistributive across the population to provide all individuals with a minimum standard of living.

With the introduction of the new State Pension in April 2016, all individuals will have a starting/foundation amount calculated based on their entitlement built up before 6th April 2016 which will be compared to the amount they would have built up with the new State Pension. Individuals will then take forward the higher calculated amount.

26 The exception to this is with money purchase or Defined Contribution schemes, where the level of NI contribution remains unchanged, but the Government later pays a rebate into the scheme.
TOC

ASP has been available in 3 guises:
- Graduated Retirement Benefit (GRB: 1961 to 1975)
- State Earnings Related Pension Scheme (SERPS: 1978 to 2002)
- State Second Pension (S2P: From April 2002)

This provides individuals with a pension more closely related to their earnings level than the flat rate that people receive from the first tier.

Members of a Defined Benefit scheme could contract out of this pension and therefore pay lower NI contributions.

From April 2016 people are no longer able to accrue entitlement to the additional state pension or Savings Credit.

TIER 2: ADDITIONAL STATE PENSION (ASP)

Other public tier benefits include:
- Housing Benefit
- Council Tax Reduction
- Attendance allowance
- Disability living allowance

Near universal benefits include:
- Christmas bonus for recipients of bSP
- Winter fuel allowance
- Free NHS prescriptions
- Free off peak bus travel

MEANS-TESTED BENEFITS

Pension credit has 2 components:
- Guarantee Credit paid to individuals who have low incomes and low savings to provide a minimum income of £167.25 a week.
- Savings Credit paid to individuals who have made private pension provisions, or have contributed in excess of the bSP and earnings-related pension. This is a maximum of £13.72 a week. Savings Credit is abolished for people who reach pensionable age on or after 6th April 2016.
- Universal Credit may be claimed by couples where one person is below SPA and one above. The maximum rate for a couple is £114.85, though this can be topped up with earnings.
THIRD TIER Provision

The third tier is private pensions, including workplace pensions and those that are not directly funded by the state. Private pensions are generally provided through the workplace, though an individual, (for example, someone who is self-employed) can take out a private pension directly with a pension provider.

Unlike state pension contributions, private pension contributions are voluntary, though there is an element of soft compulsion through the system of automatic enrolment. Private pension contributions, from the employer and/or the individual, fund designated pensions for the individual. The primary aim of private pensions is to redistribute income across an individual’s lifetime.

As with state provision, private pension provision is complicated. The legislative framework has been altered over time, adding layers of new arrangements to those already in place. In addition, because individuals have varied employment histories, many will retire with a number of pensions arising from both employer-sponsored schemes and individual arrangements. The benefits from private pension schemes vary depending on scheme rules and structure.

This section will first give a summary of Defined Benefit (DB) and Defined Contribution (DC) schemes. These are the overall structures of almost all private pensions. The difference between contract and trust based schemes are highlighted, then the different schemes for workplace and individual schemes are explained. Chart 6 simplifies the hierarchical structure of pension provision.

A scheme is different from a pension provider. One pension provider may offer thousands of different schemes as each employer will generally be offered a single “scheme” designed individually for its workforce. Therefore, two employees at different organisations may have pensions provided by the same provider while also being in separate schemes.
### The Landscape of Private Pension Provision in the UK

#### Chart 5:

<table>
<thead>
<tr>
<th>Workplace pension schemes</th>
<th>Individual pension schemes</th>
</tr>
</thead>
<tbody>
<tr>
<td>A pension scheme accessed through an employer. The employee and/or employer make contributions to the pension and this money is invested until retirement</td>
<td>A pension scheme contract taken out directly with a provider</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Trust-based schemes</th>
<th>Contract-based schemes</th>
</tr>
</thead>
<tbody>
<tr>
<td>A pension scheme governed by a board of trustees who have a fiduciary duty towards scheme members. The board of trustees manage investments on the members behalf. Traditionally these schemes were set up and run by employers</td>
<td>A pension scheme governed by a provider and an independent governance committee where a contract exists between the individual scheme member and the provider</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Defined Benefit schemes</th>
<th>Defined Contribution schemes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trust-based pension schemes run by an employer which offers pension benefits based on salary during working life</td>
<td>Trust or contract-based pension schemes run by a third party in which pension contributions are invested individually and benefits depend on pot size at withdrawal and method of accessing savings (e.g. drawdown vs. annuity)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Final Salary or Career Average schemes</th>
<th>Group personal pension schemes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trust-based pension schemes run by an employer which offers pension benefits based on salary during working life</td>
<td>Contract-based, Defined Contribution pension scheme run by a pension provider, designed for a group of employees working for a single employer (includes Stakeholder Schemes)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>DC trust schemes</th>
<th>(Individual) Personal pension schemes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trust-based, Defined Contribution pension scheme run by a single employer</td>
<td>Contract-based, Defined Contribution pension scheme run by a pension provider, designed for a single individual</td>
</tr>
</tbody>
</table>
# SUMMARY OF PUBLIC PENSIONS TIERS

## TIER 1: STATE PENSION

Contributory pension with a flat rate of £155.65 a week for individuals who have 35 qualifying years. People will also need a minimum of 10 qualifying years to qualify for any state pension.

Redistributive across the population to provide all individuals with a minimum standard of living.

With the introduction of the new single-tier State Pension in April 2016, all individuals will have a starting/foundation amount calculated based on their entitlement built up before 6th April 2016 which will be compared to the amount they would have built up with the single-tier pension. Individuals will then take forward the higher calculated amount.

## TIER 2: ADDITIONAL STATE PENSION

This provides individuals with a pension more closely related to their earnings level than the flat rate that people receive from the first tier.

3 guises:
- Graduated Retirement Benefit (GRB: 1961 to 1975)
- State Earnings Related Pension Scheme (SERPS: 1978 to 2002)
- State Second Pension (S2P: From April 2002)

Members of a Defined Benefit scheme could contract out of this pension and therefore pay lower NI contributions.

With the nSP, from April 2016 people are no longer able to accrue entitlement to the additional state pension or Savings Credit.

## MEANS TESTED BENEFITS

Pension credit has 2 components:
- Guarantee Credit paid to individuals who have low incomes and low savings to provide a minimum income of £151.20 a week.
- Savings Credit paid to individuals who have made private pension provisions, or have contributed in excess of the BSP and earnings-related pension. This is a maximum of £14.82 a week. Savings Credit is abolished for people who reach pensionable age on or after 6th April 2016.

Other public tier benefits include:
- Housing Benefit
- Council Tax Reduction
- Attendance allowance
- Disability living allowance
- Carers Allowance

Near universal benefits include:
- Christmas bonus for recipients of BSP
- Winter fuel allowance
- Free NHS prescriptions
- Free off peak bus travel
## Defined Benefit and Defined Contribution Pension Schemes

TABLE 3 explains the differences between Defined Benefit and Defined Contribution schemes.

<table>
<thead>
<tr>
<th>Question</th>
<th>Defined Benefit (DB)</th>
<th>Defined Contribution (DC)</th>
</tr>
</thead>
<tbody>
<tr>
<td>How much do members contribute?</td>
<td>Contributions are varied in order to ensure that the level of promised benefits are reached.</td>
<td>Contributions are usually expressed as a percentage of salary or total earnings. The rate of contribution could be a flat rate or could be tiered by age and/or length of service and/or seniority and/or level of earnings.</td>
</tr>
<tr>
<td>How much do members receive in retirement?</td>
<td>A DB pension scheme promises a specific level of benefit when an individual retires. Employers make the promise and are responsible for deficits in scheme funding. The Pension Protection Fund (Appendix 13) was set up in April 2005 to protect members in DB schemes.</td>
<td>A DC scheme operates on the money-purchase basis with a specified rate of contributions being paid into the scheme, but with no guarantee as to the level of the benefit that will be paid out. When an individual reaches retirement, the accrued benefit is withdrawn and is used to buy a retirement product. This means the scheme member themselves often bear the risks of having a low retirement income in later life.</td>
</tr>
<tr>
<td>Where do the contributions go?</td>
<td>DB schemes operate on a pooled fund basis; all contributions are paid into a common fund, which is invested to provide all retirement benefits. In unfunded schemes, contributions are used to pay the benefits of current scheme pensioners.</td>
<td>The contributions are invested. Often there is a choice of investment funds – managed, equity, property, gilts, and overseas – and with some schemes a choice of investment manager.</td>
</tr>
<tr>
<td>What age can a member start taking their pension?</td>
<td>Schemes usually have a normal pension age of 60 or 65, but a member can generally retire early with a reduction in benefits.</td>
<td>DC members can access their pension pot at the minimum pension age.</td>
</tr>
</tbody>
</table>
This is 55, rising to age 57 in 2028. Before age 55, people can withdraw DC pension savings but will incur a tax charge of 55%.

### What influences the pot size?

In the normal course of events, the investment performance of the scheme assets has no or minimal impact on the benefits an individual receives as it falls to the scheme provider to fill the shortfall.

At retirement, the pension will depend on the accumulated fund, the amount deducted from the fund as a tax-free lump sum (which is usually up to 25% of the total fund) and the method of accessing savings. The size of the pot depends on contributions, length of saving, employer contributions, investment performance, charges and the choice of retirement product. If investment returns or retirement income product rates are poor, then the resultant pension will be lower.

### How popular are these schemes?

DB schemes are losing popularity due to the risk placed on the employer, however they are provided to public sector employees. In 2018, 12% of DB schemes were open to new members and 41% were closed to future accrual.  

Automatic enrolment into DC schemes has resulted in 84% of all employees as active members of pension schemes.

### Can members opt out of any portion of the scheme?

DB schemes were able to contract out of paying National Insurance contributions in respect of S2P up until April 2016. The Pensions Act 2007 abolished contracting-out in DC schemes from April 2012.

Employees can choose not to be automatically enrolled into a workplace pensions. This is called “opting out”.

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28 Budget 2014  
HYBRID SCHEMES: DEFINED AMBITION, SHARED RISK AND COLLECTIVE BENEFIT SCHEMES

The Pension Schemes Act 2015 introduced legislation to facilitate the development of shared risk and collective benefit schemes in the UK.

The Act defines three different categories of pension scheme based on the type of promise offered to members during the accumulation phase about the level or amount of pension benefits. This promise will either refer to all of the retirement income payable from the scheme DB, some of the retirement income or some or all of the pot (shared risk), or no promise DC. Some forms of risk-sharing schemes already existed for example, hybrid schemes (e.g., cash-balance schemes, or with-profit arrangements).

Hybrid schemes provide a mix of benefits. For example, a ‘nursery scheme’ works like a DC scheme for younger staff, but becomes related to final salary as the member gets older. Alternatives include DC schemes which guarantee that pension benefits will not fall below the level of a final salary scheme and DB schemes which cap the salary used when calculating the final benefit, incorporating a DC top-up for members who earn more than this.

The Act also includes measures to enable the provision of collective benefits using Collective Defined Contribution (CDC) schemes. These schemes are enabled for in the Act through legislation allowing for scheme assets to be used in a way that pools risks across the scheme membership, by creating a single collective fund rather than individual funds (as in individual Defined Contribution). The legislation allows for the development of new structures offering collective benefits that allow for the pooling of investment, inflation and longevity risks between members within a workplace pension structure, and allows for pensions in payment to fluctuate.

COLLECTIVE DEFINED CONTRIBUTION SCHEMES

In 2018, Royal Mail and the Communication Workers Union (CWU) announced their intention to work together with Government to introduce the necessary legislation to enable CDC. In response to the 2018 consultation on CDC, the government concluded that as thinking in this area has moved on considerably since 2015, the Pension Schemes Act 2015 ‘does not contain suitable definitions or set out an appropriate framework for our proposed approach to CDC schemes.’ As a result, new primary and secondary legislation, which will enable Royal Mail to establish its proposed CDC scheme, is expected in 2019.

Trust and contract based schemes

Schemes can have a trust or contract-based governance structure. In a contract-based arrangement, the scheme is managed and governed by the contract provider, generally an insurance company. In a trust-based scheme, a board of trustees runs the scheme in the interests of its beneficiaries.

WORKPLACE PENSION SCHEMES

Pensions provided through the employer are called workplace pensions. Workplace pension schemes can be structured as DB, DC, or hybrid/risk-sharing schemes.

Most private pension arrangements are employer-sponsored, personal pensions, or multi-employer schemes. The employer usually contributes to these schemes, and more often than not, an employee contribution is required.

The employer link may be very strong; for example, some employers set up, fund and administer their own trust-based pension scheme, or the link may be weak; for example, the employer may only give access to a scheme run and administered by a pension provider. Many schemes are arranged through single employers, although multi-employer schemes are becoming increasingly popular in the private sector and there are a few industry-wide arrangements.

GROUP PERSONAL PENSIONS (GPP) AND GROUP STAKEHOLDER PENSIONS (CONTRACT-BASED SCHEME)
Group Personal Pensions (GPP) and Group Stakeholder Pensions (GSP) are sponsored by the employer but the legal contract is still between the individual and the pension provider (Chart 7). These two types of personal pensions are collective arrangements, made for the employees of a particular employer to participate on a group basis, and so typically obtain lower management fees than individual personal pension plans.

GROUP PERSONAL PENSIONS AND GROUP STAKEHOLDER PENSIONS HAVE INDIVIDUAL TERMS FOR GROUPS OF EMPLOYEES

Chart 7

A series of individual personal pensions for groups of employees where all members have individual terms

The main advantage of a GPP compared to an individual arrangement is that charges are likely to be lower.

From April 2001, all employers with five or more employees were required to designate a stakeholder provider to which they would make payments deducted from an employee’s pay if they requested. Employers were not required to contribute prior to their automatic enrolment staging dates (explained in a later section).

The main difference between these and other types of personal pensions at the time was that management charges in each year were limited by a maximum charge cap and providers were not permitted to charge exit penalties. For people who joined a stakeholder pension after 6 April 2005, the maximum fund management charge was 1.5% for the first 10 years, thereafter reducing to 1%. For stakeholder plans that were opened before this date, the previous maximum charge of 1% continued to apply.
However, subsequent legislation has removed most of the differences between stakeholder pension schemes and other pension schemes used for automatic enrolment. Schemes used for automatic enrolment cannot charge more than 0.75% total Annual Management Charges, excluding transaction costs, for members invested in the default fund.

Though employers are no longer required to provide access to Stakeholder schemes as they were under previous legislation, they are still available for use alongside other personal pensions.

**MULTI-EMPLOYER PENSION SCHEMES (TRUST-BASED SCHEME)**
Automatic enrolment has also heralded the rise of multi-employer schemes, some of which are master-trusts.

Multi-employer schemes are schemes that offer the same terms to every member regardless of whether they join the scheme as part of a group via their employer or singly as an employee or a self-employed person (Chart 8).

**MULTI EMPLOYER PENSION SCHEMES (E.G MASTER TRUSTS) HAVE THE SAME TERMS FOR EVERY MEMBER**

Some of these schemes are DC schemes run by an insurance company or pension provider. Others are master trusts, which are DC schemes governed by a board of trustees who owe a fiduciary duty to members. These schemes may be stand-alone (such as NEST) or have the backing of a pension provider or insurance company (such as The People’s Pension and NOW: Pensions).
Personal pensions can accept transfer values from occupational pensions or other individual arrangements (including contracted-out rebates).

**PENSION SCHEMES ACT 2017 AND MASTER TRUST REGULATION**

The Pension Schemes Act 2017 was introduced on 27 April 2017. The Act introduced authorisation criteria that master trusts must satisfy. It is regulated by The Pensions Regulator (TPR). The Act increased TPR’s powers in relation to ongoing supervision of schemes; TPR may now require that trustees of an authorised Master Trust submit a ‘supervisory return’ once in any 12-month period.

**ADDITIONAL VOLUNTARY CONTRIBUTIONS**

Until April 2006, all occupational pension schemes offered the facility for employees to make Additional Voluntary Contributions (AVCs). These AVCs could either be used to purchase extra years of service – at retirement the total pension will be based on earnings and actual service plus any added years purchased – or could be invested and the resultant pension would depend on the accumulated fund and annuity rates applicable at retirement. Some companies may no longer offer AVCs following changes to pension rules in April 2006, as there are now more options for people to top up their company pension through other means.  

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32 Between April 2001 and April 2006 members of an occupational pension scheme earning less than £30,000 a year had an alternative ‘concurrency’ option. This allowed them to contribute up to £3,600 a year into a stakeholder or personal pension. The £30,000 limit applied to each employment. So for example, it was possible for someone with more than one employment to have a concurrent pension even if his or her total earnings were above £30,000.
INDIVIDUAL ARRANGEMENTS

Personal pension plans are individual arrangements (not made through an employer) based on a direct contract between the individual and a pension provider, and are contract-based (Chart 9).

INDIVIDUAL ARRANGEMENTS ARE A DIRECT CONTRACT

Chart 9

There are several types of these including stakeholder pensions and a distinct product called a personal pension. These work with the same underlying money-purchase principle as workplace pensions, but individual pensions can have higher charges due to the provider running the scheme for one person rather than a group of employers.

Until April 2001, individual personal pensions were only available to individuals while they were self-employed, or were not members of an occupational pension scheme. Legislation introducing stakeholder pensions widened access further, and from April 2006, individual pension arrangements became open to everyone under age 75.

The majority of individual pension arrangements are now subject to the charge cap, which limits the total annual cost to members whose funds are invested in the default fund to 0.75% of funds under management.

Individual contributions to private pension schemes obtain tax relief at least at an individual’s highest marginal rate (within limits). The pension fund is accumulated in a tax-favoured environment. Employers can still contribute to a personal pension and any contributions an employer makes are tax deductible and so reduce its corporation tax liability. The company also benefits from National Insurance contribution relief.
AUTOMATIC ENROLMENT INTO PENSION SCHEMES FROM 2012


Employees between age 22 and State Pension age are eligible for automatic enrolment into a scheme chosen by their employer, with employees having the right to opt-out. The annual earnings threshold above which every employee should be auto-enrolled is £10,000 in 2019/20. Contributions become payable on band earnings over £6,136 and up to a limit of £50,000 (2019/20).\(^{34}\)

Employees have the choice to “opt out” of being enrolled into a pension scheme. Approximately every 3 years, employers must repeat the automatic enrolment process so that employees who chose to opt out can revisit their decision.\(^{35}\) This is known as re-enrolment.

Automatic enrolment started in October 2012 and was rolled out in a staged process.

- **Large employers** with 250 or more employees were required to auto-enrol their eligible employees between October 2012 and February 2014.
- **Medium sized employers** with 50 to 249 employees had automatic enrolment dates between 1 April 2014 and 1 April 2015.
- **Small employers** with fewer than 50 employees had automatic enrolment dates between 1 June 2015 and 1 April 2017.
- **New employers** setting up business from 1 April 2012 and up to and including 30 September 2017 had automatic enrolment dates between 1 May 2017 and 1 February 2018.
- **All employers** were required to automatically enrol eligible employees by 1 February 2018. Any new employer setting up business from 1 October 2017 onwards was required to comply immediately if paying earnings that attract PAYE deductions in respect of any worker.

The required level of contributions that employers and employees must make into a pension scheme (if employees remain opted in) is 8% minimum total contributions of band earnings as of April 2019.\(^{36}\) This 8% is made up of a minimum 3% from the employer and the remainder from the employee and the Government (through tax relief)\(^{37}\) (Chart 10). If the employer decides to contribute the legal minimum of 3% of band earnings, then employees who do not opt out will have to contribute 4% and the Government will contribute 1% through tax relief.\(^{38}\) However, it will be up to employers to decide whether they want to contribute more. If they contribute more than 3%, that could reduce the amount that employers are required to contribute.

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\(^{34}\) www.thepensionsregulator.gov.uk/automatic-enrolment-earnings-threshold.aspx


\(^{36}\) DWP (2012) Revised implementation proposals for workplace pension reform July 2012, para 7

\(^{37}\) The tax relief may be higher for those people who pay higher-rate tax

\(^{38}\) The tax relief may be higher for those people who pay higher-rate tax
Automatic Enrolment Review panel published a report in December 2017. The report made recommendations for the future of automatic enrolment, these included, from the mid 2020s:

- Removing the lower limit on the salary for contributions, so that salary is counted for contributions from the first pound.
- Reducing the minimum age for eligibility to automatic enrolment from 22 to 18.
- Testing ways to improve pension saving participation and retirement incomes for self-employed people.

LEVEL OF CONTRIBUTIONS THAT EMPLOYERS AND EMPLOYEES MUST MAKE INTO A PENSION SCHEME TO REACH 8% MINIMUM TOTAL CONTRIBUTIONS FROM 2019

Chart 10

(Minimum employer contributions increased from 1% to 2% of band earnings will from 6 April 2018. Employer contributions increased to a minimum of 3% from 6 April 2019.\(^39\))

AUTOMATIC ENROLMENT TEST
With the introduction of automatic enrolment in 2012, the Government set an exemption test for deciding whether an employer-based pension scheme is of a high enough standard to allow the employer to be exempt from auto-enrolling eligible employees into an alternative scheme. In order to qualify as an automatic enrolment scheme, a pension scheme must:

- Allow contributions to be made by the employer.
- Be “registered”, this means the type of scheme that receives tax advantages under the Finance Act 2004.
- DC schemes must have employer contributions of at least 3%, and total contributions of at least 8%, of qualifying (band) earnings.
- DB schemes must satisfy the Test Scheme standard or an alternative DB requirement (e.g. Costs of accruals test, Money purchase quality requirement) for all active members.\(^{40}\)
- Hybrid schemes must satisfy either the money purchase requirement or the Defined Benefit requirement as appropriate according to rules set out by the Secretary of State.

CHARGE CAP
The default fund is the fund that members will automatically have their contributions invested in, unless they make an active choice to invest in a different fund.

The Occupational Pension Schemes (Charges and Governance) Regulations 2015 introduced a cap on the charges of default funds used for automatic enrolment. This cap limits the total annual cost to members whose funds are invested in the default fund to 0.75% of funds under management. The cap applies to all scheme and investment administration charges. Transaction costs (third-party costs generated when investments are sold and bought on the market) are excluded from the charge cap.\(^{41}\)

TAX TREATMENT OF PRIVATE PENSION PROVISION
The tax treatment of private pension provision is generally expressed as EET – Exempt, Exempt, Taxed (Chart 11). Contributions into a pension fund are exempt from tax, the accumulation of the fund is mainly exempt from tax and the majority of the proceeds are taxable.

As a portion of the fund sum can be taken tax-free after minimum pension age, the final ‘T’ is only partial. The accumulation is also not fully ‘E’. The extent of taxation on the fund accumulation depends on the mix of investments within the pension fund. The roll up of funds invested directly in bonds, property or cash is completely tax-free. However, since 1997, dividend income from equities has been taxed at a Corporation Tax rate, although capital gains remain tax-free.

Prior to April 2006, contributions to and benefits from pension schemes qualified for tax relief according to limits which were closely related to how much an individual earned.\(^{42}\) There were eight different regimes, depending on the type of pension scheme in operation.

The Finance Act 2004, which took effect from 6 April 2006, included a number of amendments designed to simplify the taxation of the UK private pension regime, effectively capturing all pensions under a single set of rules.\(^{43}\)

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40 Test Scheme is a scheme that provides a pension from age 65 of 1/120 x average qualifying service over the last 3 tax years before retirement for each year of qualifying service.
42 For contributions of more than £3,600 a year
TAX TREATMENT OF PRIVATE PENSION PROVISION

Chart 11

CONTRIBUTIONS - EXEMPT
Individuals receive tax relief at their highest marginal rate. These tax advantages are controlled by the Lifetime Allowance and Annual Allowance.

FUND ACCUMULATION – MAINLY EXEMPT
There is no tax on returns though tax is payable on dividend income. If returns bring a fund above the Lifetime Allowance, they may incur a tax charge on withdrawal.

PROCEEDS – TAXABLE
Up to 25% of DC savings can be taken tax-free. The remainder of people’s income in retirement from pension savings will be taxed at their marginal rate at the point of receipt.

CONTRIBUTIONS – ‘EXEMPT’
Employer contributions are paid gross and if they are treated by HM Revenue and Customs as an eligible expense, the employer will get full relief against Corporation Tax. Making pension contributions on behalf of employees has an additional tax advantage for the employer, as employers’ pension contributions are not eligible for National Insurance contributions.

In 2019/20, employee contributions up to the lower of 100% of earnings, or £40,000 (the Annual Allowance), can be offset against income tax – individuals can benefit from tax advantages is controlled by two ‘allowances’: Annual and Lifetime. These allowances apply to each individual, and across all registered pension schemes that the individual uses for providing benefits, regardless of the time of joining.

In 2019/20, employee contributions up to the lower of 100% of earnings, or £40,000 (the Annual Allowance), can be offset against income tax – individuals can benefit from tax advantages in some cases, full relief is available immediately whereas in other cases, basic rate relief is given immediately and higher rate relief is reclaimed through the end-of-year tax return.

An individual can make contributions to any number of private pension schemes and receive tax relief on the amount saved in that year up to the Annual Allowance (AA). The AA for 2019/20 is £40,000.

Contributions above this level are taxed at an individual’s marginal tax rate.

From April 2016, the Government introduced a taper to the Annual Allowance. For every £2 over an individual’s adjusted income of £150,000 to £210,000, £1 is deducted from their Annual Allowance (Chart 12). This means an individual earning £210,000 or over can receive tax relief on contributions up to £10,000, and is then taxed at their marginal rate.

44 Although exemptions to the Lifetime Allowance are available to protect existing rights
45 In the 2017 Scottish budget, the Scottish government implemented Scotland-specific income tax rates which are reflected in the tax relief on the pension contributions that can be claimed in Scotland. More information can be found here: https://www.gov.uk/government/publications/pension-schemes-relief-at-source-for-scottish-income-tax-newsletter-february-2018/pension-schemes-relief-at-source-for-scottish-income-tax-newsletter-february-2018
Upon accessing benefits in retirement, an individual’s total pension savings will be tested against a Lifetime Allowance (LTA), whose purpose is to regulate the amount of tax relief individuals get over their working life. If the value of the pension saving at this time is above the LTA (£1.055 million for 2019/20, up from £1.03 million in 2018/19),\(^{47}\) there is an additional tax of 25% if the benefits are taken as a pension or 55% if they are taken as a lump sum.\(^ {48}\)

**FUND ACCUMULATION – MAINLY ‘EXEMPT’**

The pension fund accumulates in a tax-favoured environment – there is no tax on interest or income received gross and no tax on any realised capital gains. However, since 1997 pension funds have not been able to reclaim Advance Corporation Tax (ACT) on UK dividends.\(^ {49}\)

From April 2006, an individual can build up their pension funds tax-free until the total exceeds the Annual Allowance in any given year or the LTA.

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\(^{49}\) PPI (2005) Briefing Note Number 22 Is £5 billion being taken from pension funds each year? www.pensionspolicyinstiute.org.uk/default.asp?p=124&publication=0193
PROCEEDS – MAINLY ‘TAXABLE’

From age 55, up to 25% of Defined Contribution pension savings can be taken as a tax-free lump sum. The remainder of the fund can be withdrawn flexibly or some or all of it can be used to purchase a retirement income product such as a lifetime, fixed or flexible annuity, an income drawdown product, or another product that offers income, savings and/or insurance. Because of the newness of the policy of flexible access, it is not yet known exactly how many different products might be available or what they will look like. People’s income in retirement from pension savings is taxed at their marginal rate at the point of receipt.

Pension funds in excess of the LTA can still be taken as pension benefit, but they are subject to a different tax rate. When taken as a cash lump sum, the excess is subject to 55% tax. When taken as a pension benefit, the excess is subject to 25% tax, with the income payments taxable as earned income.

DEATH PRIOR TO RETIREMENT

If an individual dies before converting their pension savings into an income, the accumulated fund, plus any insured lump sum death benefit, can be paid out tax-free up to the member’s available LTA. Inherited pension savings (with the exception of lifetime annuities without capital guarantees) are tax-free if the fund-holder dies under the age of 75 with uncrystallised funds or funds in a drawdown account. Inherited pension savings are taxed at marginal rate if the fund-holder dies over the age of 75 with uncrystallised funds or funds in a drawdown account. Inherited pensions are taxed at 45% if the fund-holder dies over the age of 75 and the beneficiary takes it as a lump sum (those taking a lump sum in these circumstances are taxed at their marginal rate).

WITHDRAWING RETIREMENT INCOME

With both State Pension and DB Pension schemes, there is some degree of certainty about the level of income an individual will receive once pension payments commence.

In comparison, the actual level of income from a DC scheme cannot be predicted in advance. The level of pension provided will depend on the method of access, on market conditions and, in some cases, may not constitute a “pension” but rather a series of flexible withdrawals as and when desired by the fund holder.

Withdrawal of pension savings has had various policy changes over the years. Please refer to Appendix 14, which discusses these changes in more detail.

PEOPLE CAN NOW ACCESS DC PENSION SAVINGS FLEXIBLY FROM AGE 55

Until June 2010, individuals with DC pensions were effectively required to annuitise any remaining private pension savings (after taking an optional 25% tax-free lump sum) by age 75. As a response to calls for more flexibility, the Government removed the effective requirement to use private pension savings to purchase an annuity by age 75. The Government’s stated policy objective is to make pension saving more attractive by giving individuals greater choice over how they provide a retirement income for themselves.

The options open to people with DC savings are limited only by the products available and the amount of savings people have. They are also governed by taxation.

50 www.gov.uk/tax-on-pension-death-benefits
51 For more information on pre-Freedom and Choice arrangements, see Historical Annex
52 www.hm-treasury.gov.uk/d/consult_age_75_annuity_responses.pdf

Those with DB pension savings may not use flexible access unless they transfer their DB entitlement into a DC scheme first. Some DB schemes in the public sector do not allow transfers.
People with DC savings may, at age 55, do one or a combination of the following, (though this list is not exhaustive as the retirement income market is still evolving in light of the new policy):

- **Withdraw the total fund** (25% tax-free, the remainder taxed).
- Leave their pension fund invested and withdraw unlimited amounts, taxed at an individual’s marginal rate. This is known as an **uncrystallised funds pension lump sum** because the member does not “crystallise” their pension by buying a retirement product.
- Purchase a product such as **longevity insurance**.
- Purchase an annuity. A lifetime annuity is a retirement income product that pays an income from the date of purchase until the date of death. There are many different types of annuity which are explained in Appendix 15.
- Purchase an income drawdown retirement **income product**. An income drawdown means that the pension fund remains invested and benefits from investment growth, but an individual can withdraw an income from it until the fund is depleted.
- From April 2015, all new drawdown arrangements were classified as flexi-access. Individuals over 55 can take an unlimited amount of money from their fund without the restrictions of capped and flexible drawdown.53

APPENDIX 1: ELIGIBILITY FOR STATE PENSION

The State Pension is based on an individual’s National Insurance (NI) contribution record (Chart A1.1). Any tax year in which an individual makes, or is credited with making, sufficient NI contributions is known as a qualifying year.

Employees make Class 1 contributions when their weekly earnings exceed the ‘Primary Threshold’ (PT) of £166 a week.\(^{54}\) If they earn less than the PT but more than the ‘Lower Earnings Limit’ (LEL) of £118 a week,\(^ {55}\) then they do not make Class 1 contributions but are credited for the State Pension.\(^ {56}\) The self-employed make flat rate Class 2 contributions of £3.00 a week.\(^ {57}\) Class 3 voluntary contributions, of £15.00 a week,\(^ {58}\) are paid by those who wish to protect their entitlement and have not paid enough Class 1 or Class 2 contributions. Class 3 payments must generally be made within 6 years from the end of the tax year for which payment is being made.\(^ {59}\)

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56 From April 2011
58 Special Class 2 rates apply for fishermen and volunteer development workers. The self-employed also make class 4 contributions, which are earnings-related but do not affect bSP entitlement.
People were permitted to make back payments for more than 6 years if the payments were for the tax years 1996/1997 through to 2001/2002, and these payments were made by April 2009 or April 2010 depending on when people reach SPa. For detailed explanation www.hmrc.gov.uk/ni/volcontr/when-top-up.htm
### Chart A1.1

#### HOW NATIONAL INSURANCE CONTRIBUTIONS (NICs) WORK

<table>
<thead>
<tr>
<th>NIC class</th>
<th>Who pays this class of NICs</th>
<th>What this entitles people to</th>
</tr>
</thead>
<tbody>
<tr>
<td>Class 1</td>
<td>Paid by employers at a rate of 13.8% and employees aged between 16 and SPa who earn over the Primary Threshold (PT) at a rate of 12% and at a rate of 2% for earnings over the Upper Earnings Limit (UEL). People who earn at or above the Lower Earnings Limit (LEL) (£118 per week) but below the PT (£166 per week) are not required to pay but are treated as having paid NICs.</td>
<td>Each qualifying year counts towards an individual’s pension entitlement and is used to calculate how much State Pension they will receive. People who earn below the LEL do not accrue entitlement to State Pension.</td>
</tr>
<tr>
<td>Class 2</td>
<td>Paid by people who are self-employed and earn more than £6,365 a year pay NI at a fixed rate of £3.00 a week. People who earn less than £5,965 a year can no longer apply for exemption in the form of a Small Earnings Exception (SEE) certificate, however for those with profits from self-employment which are less than the small profits threshold (£6,365), no class 2 NI contributions will be due.</td>
<td>Each Class 2 contribution is treated as one week of earnings at the LEL.</td>
</tr>
<tr>
<td>Class 3</td>
<td>Voluntary contributions of £14.25 a week that people can pay to fill gaps in their contribution record.</td>
<td>Can fill in gaps of full or partial years in order to make those years qualifying years for State Pension entitlement.</td>
</tr>
<tr>
<td>Class 4</td>
<td>Additional contributions paid by self-employed people (as well as Class 2 NICs) at a rate of 9% on profits between £8,632 and £50,000 (Lower Profits Limit and Upper Profits Limit) and 2% on profits above the £50,000.</td>
<td>Does not count towards qualifying years.</td>
</tr>
</tbody>
</table>

There are many activities that can credit someone into the new State Pension without their having to pay contributions. Credit will be given if, for instance, an individual is entitled to:

- Statutory Sick Pay
- Statutory Maternity, Paternity or Adoption Pay
- Child Benefit
- Jobseekers Allowance
- Employment and Support Allowance
- Unemployability Supplement or Allowance
- Carer’s Allowance
- Universal Credit
- Jury Service

Credits are also given for men aged between women’s SPa and age 65 with incomes below a certain level, to individuals who have been wrongly imprisoned and for time spent doing Jury Service.
Home Responsibilities Protection (HRP) was introduced in 1978 and, for people reaching SPa before April 2010, reduced the number of years of contributions required to secure a full State Pension. Protection was given for those complete tax years where an individual was caring for children or an older or a disabled person. HRP was replaced by National Insurance credits from 6th April 2010, however people may still apply for HRP if they were caring for a sick or disabled person or were a foster carer before April 2010.

There were some changes in the Pensions Act 2007 that affected people who reach SPA between 6 April 2010 and April 2016. These people:

- Were able to earn positive credits towards basic State Pension (bSP) rather than HRP reductions. The outcome for individuals under a credit system is more generous and simplifies the way entitlement is calculated.
- Only needed 30 qualifying years to be eligible for the full bSP, while people who reached SPa before 6 April 2010 still need to have contributed for 39 years (for women) or 44 years (for men) to qualify for a full bSP.
- Receive a proportion of the full bSP for every contributing year, as the 25% minimum contribution limit was abolished.

Carers now receive weekly Carer's Credits for any week in which they are:

- Awarded child benefit; or
- A foster parent for a child under the age of 12; or
- Engaged in caring within the meaning given in regulations (people caring for one sick or severely disabled person for 20 hours or more a week will qualify for credit, subject to an appropriate validation process).

This change means that in any year, individuals can combine caring credits with NI contributions to build up a qualifying year. Credits for people who are caring for children are awarded until the youngest child reaches 12 years.

Grandparents of working age who care for grandchildren for 20 hours or more a week are also eligible to receive caring credits that count towards their State Pension entitlement.

PEOPLE REACHING STATE PENSION AGE BEFORE 2010

For men who reached SPa before 6 April 2010, the full bSP of £129.20 a week is payable with at least 44 qualifying years of National Insurance contributions. For women born prior to 6 April 1950 the full bSP is payable with at least 39 qualifying years.

A proportionate benefit is payable if the number of qualifying years is less than that needed for the maximum. For example, a woman who retired before 6 April 2010 with a 30 year contribution record currently receives a bSP of £99.38 a week ((30/39) multiplied by £129.20). However, if the number of qualifying years at retirement was less than 25% of the amount required for a maximum bSP then no bSP benefit is payable, for a person who reached SPa before 6 April 2010.

If a person cared for a child until the child reached age 16 the requirement for a maximum bSP would reduce from 39 qualifying years to 24. HRP did not give complete protection, as it did not reduce the number of qualifying years required for a full bSP below 20 years.

60 https://www.gov.uk/state-pension/eligibility
61 Assuming no Home Responsibilities Protection is awarded
62 Although most recipients are women, HRP is unisex - it is available to the person to whom child benefit is payable
CLASS 3A VOLUNTARY NATIONAL INSURANCE CONTRIBUTIONS

Class 3A National Insurance contributions were designed to help those people who have not been able to build up much additional State Pension but reach SPa before the introduction of the new State Pension on the 5th April 2016.

People were able to make Class 3A contributions during an 18-month period, starting in October 2015.

Each Class 3A contribution acquired a unit of extra pension which increased the individual’s additional State Pension by £1 a week up to a cap of £25 a week.

The price was set at an ‘actuarially fair’ rate and was therefore lower for older pensioners than younger pensioners.
Table A2.1 compares the effects of increases in SPA for women under the Pensions Act 2011 provisions, compared to previous legislation, according to birth date.

### TABLE A2.1: COMPARING THE EFFECTS OF PENSIONS ACT 1995 AND PENSIONS ACT 2011 PROVISIONS ON WOMEN’S SPA

<table>
<thead>
<tr>
<th>Date of Birth</th>
<th>Pensions Act 1995</th>
<th>Pensions Act 2011</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>State Pension Date</td>
<td>State Pension age</td>
</tr>
<tr>
<td>6 Jan 1954 - 5 Feb 1954</td>
<td>6 Nov 2017</td>
<td>63 yrs 10mths - 63 yrs 9mths</td>
</tr>
<tr>
<td>6 Mar 1954 - 5 Apr 1954</td>
<td>6 Mar 2018</td>
<td>64 yrs 0mths - 63 yrs 11mths</td>
</tr>
<tr>
<td>6 Apr 1954 - 5 May 1954</td>
<td>6 May 2018</td>
<td>64 yrs 1mths - 64 yrs 0mths</td>
</tr>
<tr>
<td>6 May 1954 - 5 Jun 1954</td>
<td>6 Jul 2018</td>
<td>64 yrs 2mths - 64 yrs 1mths</td>
</tr>
<tr>
<td>6 Jun 1954 - 5 Jul 1954</td>
<td>6 Sep 2018</td>
<td>64 yrs 3mths - 64 yrs 2mths</td>
</tr>
<tr>
<td>6 Jul 1954 - 5 Aug 1954</td>
<td>6 Nov 2018</td>
<td>64 yrs 4mths - 64 yrs 3mths</td>
</tr>
<tr>
<td>6 Aug 1954 - 5 Sep 1954</td>
<td>6 Jan 2019</td>
<td>64 yrs 5mths - 64 yrs 4mths</td>
</tr>
<tr>
<td>6 Sep 1954 - 5 Oct 1954</td>
<td>6 Mar 2019</td>
<td>64 yrs 6mths - 64 yrs 5mths</td>
</tr>
<tr>
<td>6 Oct 1954 - 5 Nov 1954</td>
<td>6 May 2019</td>
<td>64 yrs 7mths - 64 yrs 6mths</td>
</tr>
</tbody>
</table>

For those born between November 1954 and April 1960, SPA is 66 years old.

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64 For more information on changes to SPAs that have already occurred, see Historical Annex
### TABLE A2.2:
THE INCREASE IN SPa FROM AGE 66 TO 67 FOR BOTH MEN AND WOMEN

<table>
<thead>
<tr>
<th>Date of Birth</th>
<th>State Pension age</th>
</tr>
</thead>
<tbody>
<tr>
<td>6 April 1960 – 5 May 1960</td>
<td>66 years and 1 month</td>
</tr>
<tr>
<td>6 May 1960 – 5 June 1960</td>
<td>66 years and 2 months</td>
</tr>
<tr>
<td>6 June 1960 – 5 July 1960</td>
<td>66 years and 3 months</td>
</tr>
<tr>
<td>6 July 1960 – 5 August 1960</td>
<td>66 years and 4 months</td>
</tr>
<tr>
<td>6 August 1960 – 5 September 1960</td>
<td>66 years and 5 months</td>
</tr>
<tr>
<td>6 September 1960 – 5 October 1960</td>
<td>66 years and 6 months</td>
</tr>
<tr>
<td>6 October 1960 – 5 November 1960</td>
<td>66 years and 7 months</td>
</tr>
<tr>
<td>6 November 1960 – 5 December 1960</td>
<td>66 years and 8 months</td>
</tr>
<tr>
<td>6 December 1960 – 5 January 1961</td>
<td>66 years and 9 months</td>
</tr>
<tr>
<td>6 January 1961 – 5 February 1961</td>
<td>66 years and 10 months</td>
</tr>
<tr>
<td>6 February 1961 – 5 March 1961</td>
<td>66 years and 11 months</td>
</tr>
<tr>
<td>6 March 1961 – 5 April 1977</td>
<td>67th Birthday</td>
</tr>
</tbody>
</table>

### TABLE A2.3:
THE INCREASE IN SPa FROM 67 TO 68 FOR BOTH MEN AND WOMEN

<table>
<thead>
<tr>
<th>Date of Birth</th>
<th>State Pension age</th>
</tr>
</thead>
<tbody>
<tr>
<td>6 April 1977 – 5 May 1977</td>
<td>6 May 2044</td>
</tr>
<tr>
<td>6 May 1977 – 5 June 1977</td>
<td>6 July 2044</td>
</tr>
<tr>
<td>6 June 1977 – 5 July 1977</td>
<td>6 September 2044</td>
</tr>
<tr>
<td>6 July 1977 – 5 August 1977</td>
<td>6 November 2044</td>
</tr>
<tr>
<td>6 August 1977 – 5 September 1977</td>
<td>6 January 2045</td>
</tr>
<tr>
<td>6 September 1977 – 5 October 1977</td>
<td>6 March 2045</td>
</tr>
<tr>
<td>6 October 1977 – 5 November 1977</td>
<td>6 May 2045</td>
</tr>
<tr>
<td>6 November 1977 – 5 December 1977</td>
<td>6 July 2045</td>
</tr>
<tr>
<td>6 December 1977 – 5 January 1978</td>
<td>6 September 2045</td>
</tr>
<tr>
<td>6 January 1978 – 5 February 1978</td>
<td>6 November 2045</td>
</tr>
<tr>
<td>6 February 1978 – 5 March 1978</td>
<td>6 January 2046</td>
</tr>
<tr>
<td>6 March 1978 – 5 April 1978</td>
<td>6 March 2046</td>
</tr>
<tr>
<td>6 April 1978 onwards</td>
<td>68th Birthday</td>
</tr>
</tbody>
</table>
### APPENDIX 3: IMPACT OF INDEXATION OF THE STATE PENSION

**TABLE A3.1: Historical Uprating of bSP in relation to National Average Earnings (NAE)**

<table>
<thead>
<tr>
<th>Date</th>
<th>bSP – Weekly Amount</th>
<th>Adjusted to April 2019 prices</th>
<th>Weekly National Average Earnings</th>
<th>bSP as a percentage of NAE</th>
</tr>
</thead>
<tbody>
<tr>
<td>October 1972</td>
<td>£6.75</td>
<td>£87.47</td>
<td>£32.00</td>
<td>21.1%</td>
</tr>
<tr>
<td>July 1974</td>
<td>£10.00</td>
<td>£103.90</td>
<td>£41.70</td>
<td>24.0%</td>
</tr>
<tr>
<td>November 1977</td>
<td>£17.50</td>
<td>£106.44</td>
<td>£70.20</td>
<td>24.9%</td>
</tr>
<tr>
<td>November 1979</td>
<td>£23.30</td>
<td>£111.74</td>
<td>£89.60</td>
<td>26.0%</td>
</tr>
<tr>
<td>November 1982</td>
<td>£32.85</td>
<td>£114.82</td>
<td>£136.50</td>
<td>24.1%</td>
</tr>
<tr>
<td>April 1987</td>
<td>£39.50</td>
<td>£112.11</td>
<td>£198.90</td>
<td>19.9%</td>
</tr>
<tr>
<td>April 1992</td>
<td>£54.15</td>
<td>£112.72</td>
<td>£304.60</td>
<td>17.8%</td>
</tr>
<tr>
<td>April 2000</td>
<td>£67.50</td>
<td>£114.65</td>
<td>£425.10</td>
<td>15.9%</td>
</tr>
<tr>
<td>April 2001</td>
<td>£72.50</td>
<td>£121.01</td>
<td>£449.70</td>
<td>16.1%</td>
</tr>
<tr>
<td>April 2002</td>
<td>£75.50</td>
<td>£124.16</td>
<td>£472.10</td>
<td>16.0%</td>
</tr>
<tr>
<td>April 2003</td>
<td>£77.45</td>
<td>£123.50</td>
<td>£487.10</td>
<td>15.9%</td>
</tr>
<tr>
<td>April 2004</td>
<td>£79.60</td>
<td>£123.85</td>
<td>£498.20</td>
<td>16.0%</td>
</tr>
<tr>
<td>April 2005</td>
<td>£82.05</td>
<td>£123.73</td>
<td>£516.40</td>
<td>15.9%</td>
</tr>
<tr>
<td>April 2006</td>
<td>£84.25</td>
<td>£123.88</td>
<td>£534.90</td>
<td>15.8%</td>
</tr>
<tr>
<td>April 2007</td>
<td>£87.30</td>
<td>£122.80</td>
<td>£549.80</td>
<td>15.9%</td>
</tr>
<tr>
<td>April 2008</td>
<td>£90.70</td>
<td>£122.46</td>
<td>£574.30</td>
<td>15.8%</td>
</tr>
<tr>
<td>April 2009</td>
<td>£95.25</td>
<td>£130.12</td>
<td>£587.30</td>
<td>16.2%</td>
</tr>
<tr>
<td>April 2010</td>
<td>£97.65</td>
<td>£126.63</td>
<td>£598.30</td>
<td>16.3%</td>
</tr>
<tr>
<td>April 2011</td>
<td>£102.15</td>
<td>£125.91</td>
<td>£602.60</td>
<td>17.0%</td>
</tr>
<tr>
<td>April 2012</td>
<td>£107.45</td>
<td>£128.02</td>
<td>£607.10</td>
<td>17.7%</td>
</tr>
<tr>
<td>April 2013</td>
<td>£110.15</td>
<td>£127.56</td>
<td>£620.20</td>
<td>17.8%</td>
</tr>
<tr>
<td>April 2014</td>
<td>£113.10</td>
<td>£127.80</td>
<td>£620.80</td>
<td>18.2%</td>
</tr>
<tr>
<td>April 2015</td>
<td>£115.95</td>
<td>£129.85</td>
<td>£627.00</td>
<td>18.5%</td>
</tr>
<tr>
<td>April 2016</td>
<td>£119.30</td>
<td>£131.86</td>
<td>£644.90</td>
<td>18.5%</td>
</tr>
<tr>
<td>April 2017</td>
<td>£122.30</td>
<td>£130.58</td>
<td>£661.10</td>
<td>18.5%</td>
</tr>
<tr>
<td>April 2018</td>
<td>£125.95</td>
<td>£130.11</td>
<td>£685.30</td>
<td>18.4%</td>
</tr>
<tr>
<td>April 2019</td>
<td>£129.20</td>
<td>£129.20</td>
<td>£701.06</td>
<td>18.4%</td>
</tr>
</tbody>
</table>
## TABLE A3.2: PROJECTED LEVEL OF nSP COMPARED TO AVERAGE EARNINGS

<table>
<thead>
<tr>
<th>Tax Year</th>
<th>bSP - Weekly Amount (Projected)</th>
<th>Weekly National Average Earnings (Projected)</th>
<th>Projected bSP as a percentage of NAE</th>
</tr>
</thead>
<tbody>
<tr>
<td>2019</td>
<td>£168.60</td>
<td>£701</td>
<td>24.0%</td>
</tr>
<tr>
<td>2020</td>
<td>£173.15</td>
<td>£719</td>
<td>24.1%</td>
</tr>
<tr>
<td>2025</td>
<td>£204.05</td>
<td>£846</td>
<td>24.1%</td>
</tr>
<tr>
<td>2030</td>
<td>£255.56</td>
<td>£1,039</td>
<td>24.6%</td>
</tr>
<tr>
<td>2035</td>
<td>£320.06</td>
<td>£1,277</td>
<td>25.1%</td>
</tr>
<tr>
<td>2040</td>
<td>£400.84</td>
<td>£1,568</td>
<td>25.6%</td>
</tr>
<tr>
<td>2045</td>
<td>£502.01</td>
<td>£1,926</td>
<td>26.1%</td>
</tr>
</tbody>
</table>

## TABLE A3.3: PROJECTED UPRATING OF bSP UNDER THE TRIPLE LOCKED SYSTEM

<table>
<thead>
<tr>
<th>Tax Year</th>
<th>bSP - Weekly Amount (Projected)</th>
<th>Weekly National Average Earnings (Projected)</th>
<th>Projected bSP as a percentage of NAE</th>
</tr>
</thead>
<tbody>
<tr>
<td>2019</td>
<td>£129.20</td>
<td>£701</td>
<td>18.4%</td>
</tr>
<tr>
<td>2020</td>
<td>£132.69</td>
<td>£719</td>
<td>18.4%</td>
</tr>
<tr>
<td>2025</td>
<td>£156.37</td>
<td>£846</td>
<td>18.5%</td>
</tr>
<tr>
<td>2030</td>
<td>£195.84</td>
<td>£1,039</td>
<td>18.8%</td>
</tr>
<tr>
<td>2035</td>
<td>£245.26</td>
<td>£1,277</td>
<td>19.2%</td>
</tr>
<tr>
<td>2040</td>
<td>£307.17</td>
<td>£1,568</td>
<td>19.6%</td>
</tr>
<tr>
<td>2045</td>
<td>£384.69</td>
<td>£1,926</td>
<td>20.0%</td>
</tr>
</tbody>
</table>

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65 PPI modelling, assumes triple lock remains in place beyond the current parliament
APPENDIX 4: CATEGORIES OF BASIC STATE PENSION

Prior to April 2016 and the introduction of the new State Pension, there were five categories the basic State Pension (bSP) provided:

- Category A was based on the individual’s contributions
- Category B was based on a spouse’s or civil partner’s qualifying years
- Category C was non-contributory, and was payable to widows of men who were over age 65 on 5 July 1948
- Category D was non-contributory and was payable to people over age 80 who satisfied certain residency conditions and failed to qualify for a category A or B pension, or received less than the non-contributory rate
- Age Addition was non-contributory and was payable to all recipients of State Pensions aged 80 or above

CATEGORY A PENSION

Category A pension was contributory and based on the individual’s contribution history. Where an individual had an incomplete contribution record, and reached State Pension age (SPA) before April 2016, then the qualifying years of a spouse or former spouse (separated through either bereavement or divorce) could be substituted to provide a higher bSP.

Changes in eligibility criteria for Category A pension

For people reaching State Pension age before 6 April 2010 and for those claiming bereavement benefits, past contribution conditions continued to apply.

For those reaching SPAs between 6 April 2010 and 6 April 2016, the number of years needed to qualify for a full Category A pension was reduced from 44 years for a man and 39 years for a woman to 30 qualifying years for men and women alike. A person who had less than 30 qualifying years was entitled to a proportion of the full bSP for each qualifying year they had built up.

Parents and carers were also allowed to build up entitlement to a Category A pension through credits. Parents or guardians (awarded child benefit for a child aged under 12), a registered foster parent or a carer providing care (for one or more severely disabled persons or caring for a child under 12) reaching SPAs from 6 April 2010 until 6 April 2016 were able to build up credits towards a Category A pension.

For those reaching SPAs from 6 April 2010 to 5 April 2016, each complete year (subject to a limit) of Home Responsibilities Protection awarded under the existing rules of the scheme were converted into a qualifying year for bSP.

From 2011, grandparents of working age who cared for grandchildren for 20 hours or more a week were also eligible to build up entitlement to a Category A pension through credits.67

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66 The changes described in this section result from legislation in the Pensions Act 2007 and announcements in Budget 2009.
67 Budget 2009 speech, webarchive.nationalarchives.gov.uk/20130129110402; www.hm-treasury.gov.uk/bud_bud09_speech.htm
CATEGORY B PENSION

Category B pension was contributory and based solely on a spouse's or civil partner's qualifying years and earnings. Previously it was only payable to married women, widows and widowers but from 6 April 2010 both men and women were able to claim bSP based on their spouse's or partner's NI record if this was better than their own.

Changes to eligibility for Category B pension 68
From 6 April 2010 to 5 April 2016, people could claim a Category B pension even if their spouse had deferred their own Category A claim. Changes also allowed the spouse or partner of a carer to build up entitlement to an associated Category B pension.

Married couples
If both husband and wife had a full National Insurance contribution record then they each received a full bSP when they reached SPa. However, if the wife was entitled to less than 60% of the full bSP and she was over SPa, she may have been able to claim a composite Category A and Category B pension based on her husband's contribution record, which could increase her pension to 60% of the full rate.

Abolishment of Adult Dependency Increases
Adult Dependency Increases for dependants under SPa were abolished from 6 April 2010. 69 Provisions will be made to protect entitlements up to 5 April 2020.

Example (under the rules currently in place)
George and Elizabeth are a married couple who are both over SPa. George has a full National Insurance contribution record and receives the full bSP of £129.20 a week (Category A). In comparison Elizabeth has an incomplete record, and based on her contributions would only receive £30.15 a week (Category A). However, she can claim an additional £47.30 a week (Category B) based on George's National Insurance contribution record, giving a total weekly income of £206.65 for the couple.

After Elizabeth reached SPa, the full £206.65 is payable to the couple even if she continues to work. From that date, £129.20 would be payable to George and £77.45 would be payable to Elizabeth (£206.65 - £129.20 = £77.45).

CATEGORY C PENSION

Category C pensions are now obsolete and are being gradually phased out (there were around 7 women in receipt of Category C pension in August 2018). 70 These are payable at the rate of 60% of the full bSP to men aged over 65 on 5 July 1948 or to widows of men who were aged over 65 in July 1948.

CATEGORY D PENSION

A non-contributory pension, equivalent to the dependent adult's addition, is awarded to those who:
• are aged 80 or above, and
• have been resident in the UK for at least 10 years in the previous 20 years, and
• receive either no bSP or less than the dependent adult's addition.

This is sometimes called the 'Over 80 Pension' and it amounts to £77.45 a week in 2019/20. 70 If the person is on a reduced pension, he/she will receive the difference between £77.45 and the reduced bSP. 71

Age addition
An age addition of 25p a week is payable to all recipients of bSP aged 80 or over. When it was introduced in 1971 the full bSP was £6.00 – effectively a 4.2% enhancement. Subsequently, the age addition has not been increased, and so is now only a 0.2% enhancement.

68 Legislated in the Pensions Act 2007
69 Legislated in the Pensions Act 2007
70 DWP Stat Xplore – state pension sourced: 02.05.2019
72 www.gov.uk/over-80-pension/overview
APPENDIX 5: PENSION CREDIT

Pension Credit (PC) replaced the Minimum Income Guarantee (MIG) in October 2003. Pension Credit consists of two parts – Guarantee Credit (GC) which is similar to the MIG, and Savings Credit (SC). Since 6th April 2016, individuals can no longer receive Savings Credit. For a transitional period of 5 years (until April 2021), support will be retained for those people who may have been eligible for Savings Credit under the old system.

GUARANTEE CREDIT

Guarantee Credit (GC) replaced the Minimum Income Guarantee (MIG) in October 2003. Guarantee Credit is the name used for the means-tested income support benefit for people over the women’s SPa. It is payable from around age 65 in 2019 as a tax-free means-tested benefit, but it is only paid to those with low incomes and low savings.73

An individual or couple is eligible for GC if they74:

- Have an age equal to women’s SPa (currently around age 65½) or higher. This age is progressively increasing in line with the increase in women’s SPa, which will reach age 66 by October 2020.
- Are on a weekly income below the GC level of £167.25 a week for single pensioners and a minimum of £255.25 a week for couples (2019/20 rates), and
- Are working less than 16 hours a week (and any partner working less than 24 hours a week).

Changes around eligibility for Pension Credit

The Welfare Reform Act 2012 stipulates that an individual over the SPa will not be entitled to Pension Credit if they have a partner75 under the SPa.76 Universal Credit has been rolled out gradually with most existing claimants having been moved to Universal Credit by December 2017. Once Universal Credit is fully rolled out, the younger partner will be able to claim Universal Credit for both people in the couple until they also reach the qualifying age for GC (currently 65½, rising to age 66 by October 2020). However, Universal Credit may be paid at a lower rate than Pension Credit. This policy will take effect from 15th May 2019.

Guarantee Credit can be higher where:

- An individual (or an individual within a couple) is disabled and living either on their own or with another disabled person, or
- An individual (or an individual within a couple) is a carer getting Carer’s Allowance, or
- Where there are housing costs not fully covered by Housing Benefit.

Lower levels of benefit are paid if pensioners have savings of more than £10,00077. The assessed savings include savings and investments, and any properties that are not the beneficiary’s main home. GC is currently reduced by £1.00 a week for each £500 (or part thereof) in excess of £10,000. This is more generous than under the MIG.78

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73 Savings consist of liquid assets, such as cash, building society and bank accounts, national savings, unit trusts and shares. It does not include the value of the home.
74 Married, Civil Partners, or living together as husband and wife or as civil partners
77 https://www.gov.uk/pension-credit/eligibility
78 Under the previous legislation the MIG was reduced by £1.00 a week for each £250 in excess of £6,000.
SAVINGS CREDIT

Savings Credit (SC), which is now only available to those who reached SPa prior to April 2016, attempts to encourage saving and ensure that anyone who has made some private saving for retirement will be better off than those who have not saved.

SC pays a tax-free allowance of 60p for each £1 of income between the SC threshold and the GC threshold. This includes some income from ongoing employment, SERPS, Graduated Retirement Benefit, employer-sponsored pension schemes, personal pensions and notional income from savings. The maximum Savings Credit that can be received in 2019/20 is £13.72 for single pensioners and £15.35 for couples.

For 2019/20, the Savings Credit threshold for single pensioners is set at £144.38 a week and the Savings Credit threshold for couples is £229.67 a week.

In 2019/20, the income above which people are no longer eligible to receive SC is around £202 for single pensioners and around £294 for couples.\textsuperscript{79}

Table A5.1 below shows the impact of various levels of accrued savings for a single person receiving only the 2018/19 bSP of £125.95. In this table savings above £10,000 are considered when calculating assumed savings income.

### TABLE A5.1: INTERACTION OF ACCRUED SAVINGS WITH PENSION CREDIT

<table>
<thead>
<tr>
<th>Savings</th>
<th>Assumed Savings Income</th>
<th>GC Benefit</th>
<th>Total Weekly BSP + GC</th>
</tr>
</thead>
<tbody>
<tr>
<td>£0</td>
<td>£0.00</td>
<td>£38.05</td>
<td>£167.25</td>
</tr>
<tr>
<td>£10,000</td>
<td>£0.00</td>
<td>£38.05</td>
<td>£167.25</td>
</tr>
<tr>
<td>£12,000</td>
<td>£4.00</td>
<td>£34.05</td>
<td>£163.25</td>
</tr>
<tr>
<td>£14,000</td>
<td>£8.00</td>
<td>£30.05</td>
<td>£159.25</td>
</tr>
<tr>
<td>£16,000</td>
<td>£12.00</td>
<td>£26.05</td>
<td>£155.25</td>
</tr>
<tr>
<td>£18,000</td>
<td>£16.00</td>
<td>£22.05</td>
<td>£151.25</td>
</tr>
<tr>
<td>£20,000</td>
<td>£20.00</td>
<td>£18.05</td>
<td>£147.25</td>
</tr>
<tr>
<td>£22,000</td>
<td>£24.00</td>
<td>£14.05</td>
<td>£143.25</td>
</tr>
<tr>
<td>£24,000</td>
<td>£28.00</td>
<td>£10.05</td>
<td>£139.25</td>
</tr>
</tbody>
</table>

\textsuperscript{79} Income limits for single and pensioner couples could be higher if they qualify for a higher level of GC through severe disability, caring or housing costs.
Table A5.2 shows the interaction of Guarantee Credit with Savings Credit for various levels of assessed income for single pensioners and pensioner couples. The incomes given represent the total income considered for Pension Credit purposes. It may include, for example, basic State Pension, additional State Pension, private pension income, savings converted into notional income calculated for the pension credit calculation. Savings Credit can increase up to £13.72 a week (for a single pensioner), when income is £167.25 a week, and then begins to tail off for higher levels of income. Table A5.8 shows in bold the weekly income value at which Guarantee Credit and Savings Credit become zero because of hitting the assessed income limit.

### TABLE A5.2: INTERACTION OF INCOME WITH GC AND SC IN THE 2018/19 TAX YEAR

<table>
<thead>
<tr>
<th>Single Pensioner</th>
<th>Pensioner Couple</th>
</tr>
</thead>
<tbody>
<tr>
<td>Weekly Income</td>
<td>Guarantee Credit</td>
</tr>
<tr>
<td>£70.00</td>
<td>£97.25</td>
</tr>
<tr>
<td>£80.00</td>
<td>£87.25</td>
</tr>
<tr>
<td>£90.00</td>
<td>£77.25</td>
</tr>
<tr>
<td>£100.00</td>
<td>£67.25</td>
</tr>
<tr>
<td>£110.00</td>
<td>£57.25</td>
</tr>
<tr>
<td>£120.00</td>
<td>£47.25</td>
</tr>
<tr>
<td>£130.00</td>
<td>£37.25</td>
</tr>
<tr>
<td>£140.00</td>
<td>£27.25</td>
</tr>
<tr>
<td>£150.00</td>
<td>£17.25</td>
</tr>
<tr>
<td>£160.00</td>
<td>£7.25</td>
</tr>
<tr>
<td>£167.25</td>
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<tr>
<td>£170.00</td>
<td>£0.00</td>
</tr>
<tr>
<td>£170.00</td>
<td></td>
</tr>
<tr>
<td>£180.00</td>
<td>£0.00</td>
</tr>
<tr>
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</tr>
<tr>
<td>£200.00</td>
<td>£0.00</td>
</tr>
<tr>
<td>£201.56</td>
<td>£0.00</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
</tbody>
</table>
APPENDIX 6:
HOUSING BENEFIT

Housing Benefit (HB) is a means-tested benefit that is designed to help individuals in rented accommodation to pay for their rent. There is no set amount of HB as it is paid to single people or couples based on their income. This includes some income from employment, state and private pensions, notional income from capital and Pension Credit.

The maximum amount of benefit available is an amount equal to a person’s (or couple’s) share of the household’s rent and is paid if claimants are also eligible for Guarantee Credit. In practice, the amount of rent that can be taken into account in the calculation of HB will be restricted if the amount of rent paid by the household is considered to be excessive.\(^{80}\)

The amount of rent that is actually taken into account in the calculation of HB, after these restrictions have been applied, is called ‘eligible rent’.

HB is reduced once income reaches a personal allowance of £181.00 a week for singles and £270.60 for couples where one or both partners are aged over 65 (from April 2019).\(^{81}\) This is intentionally set to broadly equal the Guarantee Credit level (currently £167.25 a week from April 2019) plus the maximum amount of Savings Credit (£13.72 a week). As Savings Credit is taken into account for HB, this means that HB is withdrawn once an individual is no longer eligible for the Guarantee Credit.

If the claimant’s income is above the personal allowance level, then the amount of HB is reduced at the rate of 65p for every £1 of additional income. No benefit is payable if claimants have capital of more than £16,000, unless they are also eligible for Guarantee Credit.\(^{82}\) Higher personal allowances can apply for individuals who are eligible for premiums for Pension Credit.

The Welfare Reform Act 2007 legislated for the roll-out of Local Housing Allowance (LHA) across the private rented sector from 7 April 2008. LHA is a way of working out how the amount of benefit is determined and how the benefit is delivered.

The maximum amount of HB payable is the amount of rent that a particular person (or couple) pays, subject to a series of restrictions. LHA gives a claimant an allowance, based on the 30th percentile of market rents in the particular locality and on housing needs. The highest rents across the country are excluded from the calculation of the LHA in each area. Individuals can decide to live in more expensive accommodation than the allowance covers, if they can cover the difference. The previous Coalition Government made changes to housing benefit from April 2011.\(^{83}\) As a result:

- The Local Housing Allowance (LHA) is restricted to a maximum of four bedrooms for new and existing claimants.
- Weekly LHA rates are capped at £268.46 for a one-bedroom property, £311.40 for two, £365.09 for three and £429.53\(^{84}\) for a four-bedroom property. The maximum rate of Housing Benefit is limited to the rate for a four-bedroom property. There is no cap for people living in social rented or supported housing.
- LHA rates are based on the thirtieth percentile of rents of the local area rather than the median.
- From April 2013, LHA is uprated by CPI.

\(^{80}\) For example, if the contractual rent is significantly above the market level. The size of the accommodation relative to the needs of the tenant may also be considered and rents will also be compared to ‘local reference rates’, which are calculated as the midpoint of a range of rents for properties of the same size in the locality.


\(^{82}\) https://www.gov.uk/housing-benefit


\(^{84}\) https://www.gov.uk/housing-benefit/what-youll-get
The Welfare Reform Act 2012 introduced a restriction to Housing Benefit to allow for a one bedroom for each person or couple living as part of the household, with some exceptions. Pensioners are currently exempt from this; however, as the State Pension age increases the age at which people are subject to this will rise. Claimants will forego a fixed percentage of the Housing Benefit eligible rent; 14% of eligible rent for one bedroom and 25% for two or more extra bedrooms.

Deductions may be made if there is another adult living in the claimant’s home or if the claimant is single, under 35, with no dependents and renting from a private landlord.

Housing Benefit assessed under the Local Housing Allowance is paid directly to the claimant. There are some exceptions to this:

• If the claimant’s landlord is the Local Authority responsible for paying Housing Benefit, this will be given in the form of a reduction in rent due, known as rent rebate.
• If the claimant is in 8 weeks or more of rent arrears, some of the Housing Benefit must be paid directly to the landlord until the amount of arrears reduces to below 8 weeks worth of rent, unless the claimant can show that it is not in their best interests to make direct payments.
• If the claimant may have difficulty managing financial affairs or is thought unlikely to pay their rent, payments may be made directly to the landlord for up to 8 weeks while the situation is assessed.
• Payments may be made directly to the landlord if direct payments would help to keep or secure accommodation for the claimant.
• Claimants can apply for payments to be made directly to the landlord.

Under Universal Credit, which is being phased in at the moment, the housing element will be paid directly to the claimant even in the case of council tenants.

CASE STUDY
Susan is a 67 year old single woman who does not own her own home. She rents a flat costing her £85 a week. Her income from state and private pensions is £160 a week, which would entitle her to £16.62 a week from Pension Credit (made up of £7.25 from the Guarantee Credit and £9.37 from Savings Credit). If Susan had no additional savings she would be entitled to have her whole rent paid by Housing Benefit.

On the other hand, if Susan had savings of £15,000 the first £10,000 of savings is disregarded, leaving Susan £5,000 to be considered. This is converted into a “tariff income” for calculation purposes at £1 for every £500 of savings, giving Susan £10 of tariff income. This makes her income for Pension Credit calculations £170 (= £160 + £10). She would not receive income from the Guarantee Credit but her income from Savings Credit would be £12.62 a week.

Her deemed income in the calculation for her Housing Benefit entitlement would be £182.62 a week.

£182.62 = £12.62 (income from Savings Credit) + £160.00 (income from state and private pensions) + £10.00 (deemed income from savings. This is the same as the deemed income for pension credit because the calculation of tariff income from savings for housing benefit has the same savings disregard of £10,00059)

This is £1.62 above the personal allowance for Housing Benefit (£181.00 a week in 2019/20), which would reduce her income from Housing Benefit by £1.05 a week (£1.62 multiplied by 0.65). This means Susan would receive Housing Benefit worth £83.95 a week towards the cost of her rent.

If her savings were £16,000 or above, Susan would not be eligible to receive any Housing Benefit (since her savings would be above the £16,000 limit).

APPENDIX 7:  
COUNCIL TAX REDUCTION

Until April 2013, pensioners were able to access Council Tax Benefit, a means-tested benefit designed to help individuals pay their council tax. Like Housing Benefit, it was paid to singles or couples based on their income from employment, state and private pensions, notional income from capital and Savings Credit.

From April 2013, the Government has required Councils in England to design their own Council Tax Reduction Schemes. In this way, Council Tax Reduction is no longer a national entitlement. However, the Government has stated that pensioners should not be worse off under this arrangement. For the purpose of Council Tax Reduction, a pensioner is someone who has reached the qualifying age for Pension Credit, currently 65¼, rising to age 66 by October 2020. Therefore, the thresholds and maximums described below continue to apply.

The maximum amount of Council Tax Reduction payable is an amount equal to the person’s (or couple’s) liability to pay Council Tax, subject to certain restrictions. This amount is paid if the individual is eligible for Guarantee Credit.

Council Tax Reduction is reduced once income reaches a personal allowance of £181.00 a week for a single pensioner, £270.60 a week for a couple aged 65 and over, for 2019/20. If the claimant’s income is above the personal allowance level, then the amount of Council Tax Reduction is reduced at the rate of 20p for every £1 of additional income. No benefit is payable if claimants have capital of more than £16,000, unless they are also eligible for Guarantee Credit.

There was a ‘Band E restriction’ under the national Council Tax Benefit scheme. The effect of this restriction was that claimants whose property fell into Bands F, G or H were awarded Council Tax Reduction as if their property was in Band E. Some councils restrict Council Tax Reduction awards up to the value of a certain Council Tax band.

Second Adult Rebate (SAR) is a means-tested benefit but it is not assessed on the income and capital of the person liable to claim it. It aims to compensate people who pay Council Tax but who were not able to claim a single person discount because there was a second adult present in their household.

A single person discount can reduce a person’s liability to Council Tax by 25%, if they are the only adult living in the property. If a second adult is present, SAR can reduce up to 25% of the council tax paid by the claimant. A 25% rebate is paid if the second adult is in receipt of Income Support, Income-based Jobseeker’s Allowance or Pension Credit, however this amount is reduced if the second adult has higher levels of income. If the second adult’s gross weekly income is less than £193, the rebate is 15%, if it is between £193 and £249.99 the rebate is 7.5%. No rebate is awarded if their income is £250 or above.86

Whenever someone claims main Council Tax Reduction, SAR is also calculated. The claimant is then awarded whichever benefit (main Council Tax Reduction or SAR) is most advantageous to them. In practice, there are very few awards of SAR.87

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87 The DWP is unable to confirm exact figures of how many people claim SAR, and has removed estimates from their publications.
CASE STUDY
Tim and Kate are a married couple and are both above age 65. Their Council Tax liability is £12.25 a week. Their combined income from State Pensions is £260 a week, which would entitle them to £13.45 a week from Pension Credit (made up entirely of Savings Credit).

Even if they had no additional savings Tim and Kate would still not be entitled to a Council Tax rebate of 100% of their liability because their deemed income of £273.45 a week (£260 + £13.45) is above the personal allowance for couples of £270.60 a week in 2019/20. But they would be eligible to partial Council Tax Reduction.

Their deemed income is therefore £2.85 above the personal allowance, which would reduce their income from Council Tax Reduction by £0.57 a week (£2.85 multiplied by 0.2). So Tim and Kate would receive a Council Tax rebate worth £11.68 a week.

If Tim and Kate did have savings above the £16,000 limit, they would not be eligible to receive any Council Tax Reduction.
APPENDIX 8: OTHER FIRST TIER BENEFITS

INDIVIDUALLY ASSESSED BENEFITS

Disability-related benefits such as Attendance Allowance are payable if individuals satisfy the qualifying criteria – for instance:

- **Attendance Allowance (AA)** - lower rate of £58.70 from April 2019 – payable if the individual needs care during either the day or the night. Attendance Allowance (AA) can only be claimed after State Pension age. 88
- **Attendance Allowance** - higher rate of £87.65 from April 2019 – payable if the individual needs personal care during both the day and the night. 89
- **Disability Living Allowance (DLA)** – consists of two elements - a care component of between £23.20 and £87.65 a week from April 2019 for personal care, and a mobility component of between £23.20 and £61.20 a week from April 2019. DLA can only be newly claimed before age 16, although payment for continuous claims can continue after age 65. Prior to April 2013, individuals over 16 could apply for DLA. Since then it has been gradually replaced by Personal Independant Payment (PIP). Those who were already aged over 65 and in receipt of DLA in April 2016 can continue to receive payments without transitioning to Personal Independant Payment.
- **Personal Independence Payment** - PIP is replacing DLA for those people aged 16 to State Pension age. There is a staged timetable for this development; in 2013 PIP was introduced for new claimants. From 2013, DWP started to contact people aged 16 to 65 in receipt of DLA about transferring to PIP. 90 From April 2019, PIP pays between £58.70 to £87.65 for the daily living component and between £23.20 and £61.20 for the mobility component. 91
- **Carer’s Allowance** of £66.15 a week from April 2019 is payable to those spending at least 35 hours a week looking after someone receiving certain disability benefits including AA and DLA and PIP. 92

Attendance Allowance (AA) and Disability Living Allowance (DLA) and Personal Independence Payments (PIP) are tax free, are not means-tested and do not count as income for the purposes of assessing eligibility for other benefits (such as Pension Credit, Housing Benefit and Council Tax Reduction).

Carer’s Allowance is not payable to those who earn more than £123 a week (after tax and certain expenses) and may be eligibility may be affected if the individual is in receipt of some other benefits equal to or higher than the level of carer’s allowance (these are known as ‘overlapping benefits’). 93 The amount received can also be reduced if individuals receive other state benefits. Carer’s Allowance is taken into account as income for the purposes of assessing eligibility for means-tested benefits, although an individual in receipt of Carer’s Allowance may qualify for a carer premium in Pension Credit.

88 https://www.gov.uk/attendance-allowance
89 https://www.gov.uk/attendance-allowance
91 https://www.gov.uk/pip/what-youll-get
92 https://www.gov.uk/carers-allowance
93 https://www.gov.uk/carers-allowance/effect-on-other-benefits
NEAR UNIVERSAL BENEFITS

Paid irrespective of income or assets, including:

- **Christmas Bonus** - £10 for each recipient of State Pension - paid annually before Christmas.
- **Winter Fuel Payment** - £200 per household where at least one person is SPa or over, and £300 per household where at least one person is aged 80 or over - paid annually in December. The qualifying age for this benefit increases in line with SPa.
- **Free NHS prescriptions** and eye tests for those over 60.
- **Free TV Licences** for those over 75.
- **Free central heating** installed for people receiving Pension Credit and discounts for other pensioners.
- **Free off-peak nationwide bus travel** for those aged over SPa. In London, people over 60 can travel free on buses, tubes and other transport.

TAX ALLOWANCES

- The personal allowance is the amount of income receivable before income tax becomes payable. From 2017/18, all individuals regardless of date of birth have the same personal allowance. The personal allowance in 2019/20 is £12,500. This allowance is subject to the £100,000 income limit and the allowance is reduced by £1 for every £2 above the limit.
- Prior to April 2016, the personal allowance was £10,660 for people born before 6 April 1938, with less than £27,700 in earnings. Those born between 6 April 1938 and 5 April 1948 had an increased personal allowance up until 2014/15, but this has now been phased out.
- The Government removed the increased personal allowance for people born before 6 April 1938. The personal allowance for such people was frozen at £10,660 until it met the personal allowance level for those born after 5 April 1938, which occurred in April 2016.
- The married couple’s allowance provides 10% tax relief for couples where one was born before 6 April 1935. This allowance has a minimum of £3,360 and a maximum of £8,695. Where income exceeds £28,900 any married couple’s allowance is reduced at the rate of £1 for every £2 of ‘excess’ income, to the minimum of £3,360. There is no married couples allowance for those born after 6 April 1935.

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94 www.gov.uk/winter-fuel-payment
95 For people with incomes over £27,000 their personal allowance is reduced by £1 for every £2 over the £27,000 limit until it reaches the personal allowance for those born after 6 April 1948.
96 www.gov.uk/income-tax-rates
97 As announced in Budget 2012
98 This is the notional value of the married couple’s allowance to those aged under 65, which was abolished with effect from the 2000/1 tax year
APPENDIX 9: STATE SECOND PENSION (S2P)

After the new State Pension was introduced on 6th April 2016, people can no longer accrue entitlement to S2P. However, people who have already accrued entitlement will have their entitlements recognised under the new system through their additional State Pension entitlement forming part of their foundation amount.

State Second Pension (S2P) was an additional State Pension scheme introduced by the Government in 2002 under the Child Support, Pensions and Social Security Act 2000, as the successor benefit to SERPS. The aim of S2P was to target greater resources at the lower-paid than SERPS did, and to provide pension benefits for some carers and individuals with a long-term disability.

S2P was funded through National Insurance contributions on a pay-as-you-go basis. The pension was payable from SPA and was taxable. All employees were members of S2P, and earned S2P pension for any periods of employment, unless they:

• earned below the Lower Earnings Limit, or  
• were aged over SPA, or  
• were a married woman or widow paying reduced rate NI contributions, or  
• were members of a contracted-out occupational pension scheme.

No S2P was earned for periods of self-employment or unemployment.

S2P at SPA is based on band earnings. Before 6 April 2010, there were three bands. Following provisions in the 2007 Pensions Act, the former second and third bands merged. The band earnings and accrual rates were the following:

• Those earning between the Lower Earnings Limit (LEL) £5,824 a year (2015/16) and the Low Earnings Threshold (LET) of £15,300 a year (2015/16) were treated as if they earned £15,300. Benefit accrued at a flat rate of £93.60 indexed to National Average Earnings.
• Those earning between £15,300 a year and the Upper Accrual Point (UAP) of £40,040 a year (2015/16) also accrued benefit a rate of 10% of earnings within this band.
• Some carers (caring for children under 12-years old or disabled relatives) and people with a long-term illness or disability were treated as if they were employees earning at the LET.

Changes in the Pensions Act 2007 increased the number of people accruing S2P. Starting in April 2010, the changes allowed people to be deemed to be earning at the LET by combining earnings below the LET with a system of weekly credits.

The new earnings credits, of 1/52 of the qualifying earnings factor for the year, were available in respect of each week in which the person was:

• awarded child benefit for a child under 12, or  
• a foster parent, or  
• caring for someone with a qualifying disability benefit for at least 20 hours a week, or  
• entitled to Carer’s Allowance, or  
• entitled to Severe Disablement Allowance or long-term Incapacity Benefit.

99 For the current earnings limits - www.hmrc.gov.uk/rates/nic.htm  
101 Before April 2010 not all carers could accrue benefits, as they had to have cared for the entire financial year. Shorter spells of caring or those that straddle two financial years did not qualify.
APPENDIX 10: STATE SECOND PENSION (S2P) ACCRUAL

After the new State Pension was introduced on 6th April 2016, people can no longer accrue entitlement to S2P. However, people who have already accrued entitlement will have their entitlements recognised under the new system. As many pensioners and working age individuals have accrued entitlement to S2P, it is still mentioned under the current system.

Following provisions in the Pensions Act 2007, from April 2010, S2P band-earnings reduced to only two. The goal of these changes was to progressively move the S2P towards a flat rate benefit, though all S2P accrual ended after the introduction of the new State Pension. People who have already accrued entitlement will have their entitlements recognised under the new system.

The two band-earnings were the following:
- The first band was between the Lower Earnings Limit (LEL) and the Low Earnings Threshold (LET) (£5,824 to £15,300 from April 2015).
- The second band was between the LET and the Upper Accrual Point (UAP) (£15,300 to £40,040).

The accrual rate varied for each band. Until 5 April 2012, the accrual rate was 40% of earnings for the first band and 10% of earnings for the second band. From 6 April 2012, the accrual for earnings in the first band was switched to a flat rate. 102 From April 2015 to April 2016, the accrual rates for S2P were the following:
- A flat rate of £93.60 a year for earnings within the first band. This flat rate is indexed to National Average Earnings.
- A rate of 10% of earnings per year for earnings within the second band.

At retirement the State Second Pension is calculated by dividing the total of the revalued accrual by the individual's potential working life from age 16 to SPa, or from 1978 to SPa, whichever is shorter.

The upper limit of the first band (LET = £15,300) 103 increased each year in line with national average earnings. The upper limit of the second band (UAP = £40,040) was fixed.

Where earnings were below the LET, individuals were treated as if they earned at the LET. Qualifying carers or disabled people were also treated as if they earned at the LET. If individuals had earnings below the LEL (£5,824 in 2015/16), then they did not accrue rights to S2P. Table A11.1 (next page) shows the annual accrual to S2P for 2015/16 for different levels of earnings.

102 These changes were introduced by Order 189: The Social Security Pensions (Flat Rate Accrual Amount), following the provisions of the Pensions Act 2007 of moving the S2P progressively towards a flat rate benefit. www.legislation.gov.uk/uksi/2012/189/pdfs/uksi_20120189_en.pdf
103 www.legislation.gov.uk/uksi/2013/528/made
### TABLE A11.1: S2P ACCRUAL – 2015/16\(^{104}\)

<table>
<thead>
<tr>
<th>Earnings from employment</th>
<th>Band earnings</th>
<th>S2P accrual (p.a.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Carer - £0</td>
<td>-</td>
<td>£92</td>
</tr>
<tr>
<td>£3,000</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>At LEL - £5,824</td>
<td>-</td>
<td>£92</td>
</tr>
<tr>
<td>£6,024</td>
<td>£200</td>
<td>£92</td>
</tr>
<tr>
<td>£10,000</td>
<td>£4,176</td>
<td>£92</td>
</tr>
<tr>
<td>At LET - £15,300</td>
<td>£9,476</td>
<td>£92</td>
</tr>
<tr>
<td>£19,000</td>
<td>£13,176</td>
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<td>£34,300</td>
<td>£28,476</td>
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</tr>
<tr>
<td>£35,000</td>
<td>£29,176</td>
<td>£132</td>
</tr>
<tr>
<td>At UAP - £40,040</td>
<td>£34,216</td>
<td>£142</td>
</tr>
<tr>
<td>£50,000</td>
<td>£34,216</td>
<td>£142</td>
</tr>
</tbody>
</table>

104 Assumes potentially 49 years of service
APPENDIX 11: CONTRACTING-OUT – ADDITIONAL ELEMENTS ASSOCIATED WITH S2P

After the new State Pension was introduced on 6th April 2016, people can no longer accrue entitlement to Second State Pension (S2P). However, people who have already accrued entitlement will have their entitlements recognised under the new system.

The replacement of the State Earnings Related Pension Scheme (SERPS) with the S2P created some additional complications for contracting-out.

CONTRACTING-OUT INTO A DEFINED BENEFIT (DB) PENSION SCHEME

If a DB pension scheme was contracted-out then the benefits it provides must meet or exceed a minimum standard. For example, benefits must be structured in such a way that at least 90% of the membership is better off than they would have been if they had remained in SERPS/S2P. The enhancements to S2P would have forced schemes to revise their benefit structures.

At the time of the replacement of SERPS by S2P in 2002, it was decided that contracting-out would continue for both DB and Defined Contribution (DC) pension schemes on terms similar to those which applied when SERPS was in operation:

- The rebates received by the scheme would be based on the accrual rate under SERPS.
- The individual would also accrue a residual S2P benefit that is calculated as the difference between the S2P accrual and the SERPS accrual.
- Anyone earning below the Upper Earnings Threshold £32,600 (2010/11) would accrue benefits in both their occupational scheme and in S2P. The Upper Earnings Threshold was abolished after 2011 when S2P accrual was reduced to two bands.

CONTRACTING-OUT INTO A PERSONAL PENSION

For individuals who were contracted-out into a personal pension, the rebate was based on the individual’s actual earnings from employment and the actual S2P accrual rates for the different bands of earnings.

Those earning below the Low Earnings Threshold (LET) accrued S2P benefits within S2P, as the flat rate part of S2P assumed earnings at the LET. The S2P benefit is based on the difference between their actual earnings and the LET.

From April 2012 it was no longer possible to contract out of S2P using a DC occupational, stakeholder or personal pension.
APPENDIX 12: THE PENSION PROTECTION FUND

A key feature of Defined Benefit (DB) schemes is that the employer is assumed to pay sufficient contributions to ensure that the promised benefits are paid. However, in some cases employers are not able to pay the promised benefits if, for example, their scheme becomes underfunded or the employer becomes insolvent.

The Pensions Act 2004 established a Financial Assistance Scheme (FAS) to offer help to members who have lost benefits through Occupational Pension schemes that are underfunded when they begin to wind up and/or where the employer is insolvent or no longer exists. Members from under-funded pension schemes that started winding up between 1 January 1997 and 5 April 2005 are potentially eligible for help from the FAS.

The Pension Protection Fund (PPF) became operational in April 2005. It has been designed to protect members of certain eligible DB occupational schemes and the DB parts of hybrid schemes. The PPF aims to pay some of the pension to members of schemes who lose out when the employer running their scheme becomes insolvent and the pension fund is underfunded.

The PPF is managed by an independent Board, who pay compensation, calculate annual levies and oversee the investment of the fund assets.

The PPF pays out 100% of the current level of pensions already in payment, and 90% of the pension owed for people not yet receiving a pension. Pensions in payment are increased each year in line with the rise in the Consumer Prices Index (CPI) capped at 2.5%. Compensation payments are subject to an overall cap (not applicable to pensions already in payment, unless the member is younger than the scheme’s normal pension age). The standard amount of the cap is age related, for example, from April 2019 the standard amount of the cap at age 65 is £40,020.34 for current pensioners (£36,018.31 for a 65-year-old not yet receiving a pension), and is adjusted depending on the age that the pension comes into payment. These factors may mean that pensions received from the PPF are smaller than some members had expected to receive from their original scheme.

INCREASED COMPENSATION CAP FOR LONG SERVICE

From 6 April 2017, the PPF implemented an enhanced compensation cap for employees with long service. For each year of service over 20 years, the cap is uprated by 3% of the standard amount for a person of their retirement age. The enhanced cap is subject to a maximum of twice the standard amount. These new rules apply to existing and future beneficiaries of the PPF. However, while compensation will be reassessed for people currently receiving pension payments, it will not be backdated.

Compensation payments are partly funded by compulsory annual levies contributed by eligible schemes. Since 2006/7, the annual levy comprises an administration levy and a pension protection levy. The administration levy is set in statute and covers the PPF initial start-up and running costs. The pension protection levy is set by the PPF Board based on scheme and risk-based factors. Scheme-based factors take into account the level of liability owed to the scheme’s members. The risk-based element relates to a scheme’s funding level and the risk of becoming insolvent. When the PPF takes responsibility for a scheme, it will also acquire the remaining assets of that scheme to help pay for member’s compensation.

105 DWPP Pension Reform – Financial Assistance Scheme www.dwp.gov.uk/lifeevent/penret/penreform/fas/
106 Extensions to FAS were announced in December 2007. The Pensions Act 2007 provides part of those extensions and the rest will be brought forward in regulations. The changes raise the rate of assistance to 90% of accrued pension at the date of commencement of wind up, revalued to their retirement date. This will be subject to a cap of £26,000 a year. Assistance will be paid from the scheme’s normal retirement age (but not before age 60). To be eligible to get payments from FAS a person needs to be or have been a member of a qualifying pension scheme (or the survivor of such a member). The extensions to FAS remove the age criterion for eligibility. Members of qualifying schemes no longer need to have been within 15 years of their normal retirement age on or before 14 May 2004 to qualify for assistance; the new, more generous level of assistance will be received by all qualifying members, regardless of age. Schemes belonging to solvent employers may now also be eligible.
webarchive.nationalarchives.gov.uk/+; www.dwp.gov.uk/lifeevent/penret/penreform/fas/pensions-hoc-statement-17-12-07.pdf
107 Compensation cap factors 2019 (PPF)
108 http://www.pensionprotectionfund.org.uk/Pages/Compensation.aspx
APPENDIX 13:
PENSION FUND REGULATORY FRAMEWORK

The Pensions Act 2004 introduced a number of changes to the regulation of Occupational Pension schemes.\(^\text{109}\)

This included the introduction of The Pensions Regulator who replaced the Occupational Pensions Regulatory Authority in April 2005. This independent body aims to protect members of work-based private pension schemes, to promote good scheme administration practices and to reduce the likelihood of members having to claim compensation from the Pension Protection Fund.\(^\text{110}\)

The Regulator has new powers to tackle under-funding and will focus its investigative powers on schemes that are at risk from fraud or poor management and administration.

A second aim of The Pensions Regulator is to reduce the burden of regulation compliance on well-run schemes, in order to allow them more flexibility.

Most occupational pension schemes are established as trusts, so the pension scheme’s assets are managed separately from the sponsoring employer’s control. A trustee is a person or company who is responsible for running the pension scheme properly and securing members’ benefits.

The role and duties of trustees are set by various laws and acts of Parliament supported by guidance from The Pensions Regulator.\(^\text{111}\)

In addition, the Pensions Act 2004 introduced new regulations on the management and governance of pension schemes.

There are two main requirements:

- For at least a third of trustees in every scheme to be nominated and selected by members.
- Obligations of trustees to have knowledge of scheme documentation, pensions and trust law and principles of investing and funding.

One of the responsibilities of trustees is to ensure that their schemes are adequately funded. The Pensions Act 2004 replaced the minimum funding requirement (MFR) with more scheme specific requirements. Additional legislation includes:

- Trustees to publish a Statement of Funding Principles, setting out funding strategies and strategies to tackle funding deficits.
- Better information for scheme members regarding funding.


\(^{110}\) www.thepensionsregulator.gov.uk

\(^{111}\) Trustees and the Pensions Regulator www.thepensionsregulator.gov.uk/trustees/
Provisions under the Pensions Act 2004 have given trustees more flexibility in how they run their schemes, enabling them to adapt their scheme to changing circumstances. Schemes are now able to modify the benefits that members have already accrued as long as they have consulted with the members or are replacing benefits with an actuarially equivalent value.

Greater protection for scheme members has also been factored in. Sponsoring employers are now obliged to consult scheme members before making certain changes to scheme rules. The Pensions Regulator is responsible for enforcing this, with the power to issue fines for non-compliance. Changes to future pension arrangements which would require consultation include closing the scheme to new employees and changes in employer contributions.

The Occupational Pension Schemes (Charges and Governance) Regulations 2015 introduced new minimum governance standards for relevant occupational pension schemes to apply from April 2015. Trustees and managers are responsible for ensuring these are maintained. The governance standards involve requirements for trustees to ensure that default arrangements are designed in member’s best interests; financial transactions are prompt and accurate; and charges and costs are assessed for value for members.112

The Pensions Act 2014 provided for the introduction, from April 2015, of Independent Governance Committees for pension schemes which are not governed by a board of trustees (otherwise known as contract-based schemes). These committees are intended to act, to some extent, as trustees on behalf of members and assess the value for money of the services offered to members. If the schemes do not sufficiently address problems highlighted by the committee, then the committee has the power to escalate concerns to the Financial Conduct Authority.113

APPENDIX 14: WITHDRAWING RETIREMENT INCOME

Prior to April 2006, upon reaching retirement age individuals could take a 25% tax-free lump sum while leaving the rest invested in an income drawdown account, within limits. By age 75, any remaining pension pot balance had to be annuitised. Individuals with a pension pot below the trivial commutation limit were allowed to take the whole fund as a lump sum.

Between 2006 and 2010, if a person had private pension savings above the trivial commutation limit and had not opted for an annuity by the time they reached age 75 they were required to begin withdrawing their pension benefits, either by purchasing an annuity or by the additional option of an alternatively secured pension (ASP) drawdown account. ASPs were primarily designed for those who had a principled religious objection to buying an annuity, but were used by some people as a way to avoid purchasing an annuity over age 75.

From April 2011, the requirement to purchase an annuity by age 75 was removed. Between April 2011 and 6 April 2015, people over the age of 55 could choose one or a combination of following options:

- Taking a 25% tax-free cash lump sum (provided the scheme rules allowed it). If an individual’s entire pension fund was less than the trivial commutation limit (set at £30,000 from 27 March 2014), it was possible to ‘trivially commute’ and take the whole fund as a lump sum, with 25% being tax-free and the remainder taxed at their marginal rate.
- Investing some or all of their fund for some part or all of their retirement in an income drawdown account (while taking an income from it, capped at a fixed percentage of an equivalent annuity);
- Purchasing an annuity. An insurance product that pays an income from the date of purchase until the date of death;
- Withdrawing their fund in unlimited amounts provided that individuals can demonstrate a secured guaranteed lifetime pension income of at least £20,000 a year.

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114 The trivial commutation has previously been set at 1% of the Lifetime Allowance (currently £1.8m) however it has been decoupled from the Lifetime Allowance from 2012 HMT (2010) Restricting pensions tax relief through existing allowances: a summary of the discussion document responses, p. 26.
115 An annuity insures against an individual’s money running out because he or she lives longer than expected.
116 HMT (2011). Removing the Effective Requirement to Annuitise by Age 75, p.2. webarchive.nationalarchives.gov.uk/20130129110402; ww.hm-treasury.gov.uk/d/pensions_annuitisation.pdf
APPENDIX 15. ANNUITIES

Many people who retired with DC pension savings prior to April 2015 purchased an annuity and therefore they still constitute a significant proportion of income for current pensioners. Most annuities purchased prior to April 2015 were level; meaning that once the annuity is purchased, the level of income an individual receives from it is then set for the remainder of the individual’s life.

The cost of an annuity depends on the following factors:

- Long-term interest rates prevalent in the market at that time
- The age and gender of the individual
- The health and lifestyle of the individual - for example those in poor health may be able to get a higher income from their fund
- The type of benefits chosen – for example those increasing in line with RPI, or incorporating a spouse’s pension are more expensive
- Expenses of the provider, including any profit margins.

While people are no longer compelled to purchase an annuity in order to access their DC savings, there are still many annuities on the market.

- **Lifetime annuity**
  - **Level**: an annuity that provides a set level of income for the remainder of an individual’s life.
  - **Escalating annuity**: annuities with income that escalates in line with prices.
  - **Impaired life/enhanced annuity**: an annuity that pays out a higher rate for people who have a lower life expectancy due to health or lifestyle factors.
  - **Joint annuity**: Annuitants with dependents can ensure that their dependent continues to receive an income after the annuitant’s death by purchasing a joint life annuity; however joint life annuities pay out a lower rate in return for the guarantee.
- **Fixed-term annuity**: an annuity for a fixed period.
- **Deferred annuity**: an annuity that does not start to pay out income until a later date.
ACKNOWLEDGEMENTS AND CONTACT DETAILS

This document is intended to provide a description of the UK pensions system for the purpose of considering pensions policy. It should not be used to make individual pensions decisions.

Every effort has been made to avoid error, but in such a complicated field unintentional errors and omissions may remain. Please contact the PPI if any data appears to be out-of-date, or to suggest additional subjects for the appendices.

The PPI is grateful for input from Michael Martin, Sue Ward, Keith Bell and Karen Smyth in support of earlier versions of this paper.

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