PENSIONS POLICY INSTITUTE

PPI

The Pensions Primer: A guide to the UK pensions system

Historical Annex

The Pensions Primer: a guide to the UK pensions system – Historical Annex

Introduction 1

First tier: Eligibility for Basic State Pension 2

First tier: Deferral of state pensions 9

Second tier: State Earnings Related Pension Scheme (SERPS) 10

Second tier: Second State Pension (S2P) accrual – comparisons with SERPS accrual 12

Second tier: Graduated Retirement Benefit (GRB) 14

Second tier: Accessing pension savings pre-Freedom and Choice 16

Third tier: Preserved rights and protection 17

Acknowledgements and contact details 18

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Introduction

Pensions policy has been affected by a significant amount of legislative change made by successive Governments. Today's pensions system is constructed of a complicated mix of current and discontinued policies. As a result, many of today's and tomorrow's pensioners will receive income from state schemes (such as State Earnings Related Pension and Graduated Retirement Benefit) which have been discontinued or replaced with new schemes.

The PPI's reference manual: *The Pensions Primer: a guide to the UK pensions system*[1] (last updated July 2013) gives a detailed description of the current pensions system and how it operates. This is a historical annex to the guide.

This document is intended to provide information on areas of the pensions system where it is no longer possible to accrue benefits, but where accrued benefits are still payable to current and future pensioners.

The areas covered in this document are described in brief in *The Pensions Primer: a guide to the UK pensions system*, but readers can use the *Historical Annex* as a reference for more detailed discussion of these areas and of the policy changes that were made to the discontinued parts of the pension system.

[1] Available at www.pensionspolicyinstitute.org.uk

First tier: Eligibility for Basic State Pension

The Basic State Pension (BSP) is based on an individual's National Insurance (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.

Employees make Class 1 contributions when their weekly earnings exceed the 'Primary Earnings Threshold' (PET) of £146 per week.[2] If they earn less than the PET but more than the 'Lower Earnings Limit' (LEL) of £107 per week, then they do not make Class 1 contributions but are credited for the BSP.[3] The self-employed make flat–rate Class 2 contributions of £2.65 per week.[4] Class 3 voluntary contributions, of £13.25 per week, 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.[5]

There are 19 activities that can credit someone into the Basic 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 Pay, Jobseekers Allowance, Incapacity Benefit, Carer's Allowance, Severe Disablement Allowance, or if an individual is aged 16, 17 or 18, or for men aged 60 to 64.[6]

No qualifying years are earned and no credit is earned if a married woman or widow is paying reduced-rate NI contributions.[7]

Home Responsibilities Protection (HRP) was introduced in 1978 and, for people reaching SPA before April 2010, reduced the number of years of contribution required to secure a full BSP. Protection was given for those complete tax years where an individual was caring for children or an older or a disabled person.

[2] www.hmrc.gov.uk/rates/nic.htm
[3] From April 2011
[4] 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.
[5] 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 see: www.hmrc.gov.uk/nic/class3.htm
[6] House of Commons Hansard, 26 June 2006 Col 63W www.publications.parliament.uk/pa/cm200506/cmhansrd/vo060626/text/60626w0013.htm#06062622000050
[7] Between 1948 and 1978 married women could elect to pay a reduced rate of NI contributions, known as the 'Married Women's Reduced Rate Election'. By electing to pay the reduced rate, women forfeited the right to a pension based on their own contributions and instead relied on their husband's contribution record. The wife would then receive a pension once the husband reached 65 at the rate of 60% of the husband's pension. The option to elect to pay the reduced rate ceased to be available in 1977. Entitlement to the option is lost if an individual is not working for more than 2 complete tax years. Alternatively, individuals can elect to recommence paying the full rate. PPI calculations based on data provided by DWP estimate that in 2003 around 60,000 women were still paying at the reduced rate (Briefing Note 11, July 2004). This figure is likely to have reduced since 2003.

There were some changes in the Pensions Act 2007 which affected people reaching SPA from 6 April 2010. These people:

- will be able to earn positive credits towards BSP rather than HRP reductions. The outcome for individuals under a credit system is more generous and simplifies the way entitlement is calculated.
- only need 30 qualifying years to be eligible for the full Basic State Pension, while people who reached State Pension Age before 6 April 2010 still need to have contributed for 39 or 44 years to qualify for a full Basic State Pension.
- will receive a proportion of the full BSP for every contributing year, as the 25% minimum contribution limit is abolished.

For example, a person with 5 qualifying years and 10 years of HRP would, under the reduction system receive 25% of the full state pension; calculated as 5 years out of their 20 (i.e. 30 – 10 HRP) required years. Under a credit system, the same person would receive 50% of the full state pension; calculated as 15 (5 + 10 credits) years out of their required 30 years.

Carers now receive *weekly* contribution credits for any week in which they:

- are awarded child benefit; or
- are a foster parent for a child under the age of 12; or
- are engaged in caring within the meaning given in regulations (people caring for one sick or severely disabled person for 20 hours or more per 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 (down from 16 years), aligning the rules for Basic State Pension and State Second Pension (discussed in the next section).

Grandparents of working age who care for grandchildren for 20 hours or more per week are also be eligible to receive caring credits which count towards their BSP entitlement.

People reaching SPA before 2010

For men who reached State Pension Age before 6 April 2010, the full BSP of £107.45 is payable with at least 44 qualifying years from a maximum of 49. For women born prior to 6 April 1950 the full BSP is payable with at least 39 qualifying years from a maximum of 44.

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 £82.65 per week ((30/39) * £107.45).[8] 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[9] 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.

Changes in the Pensions Act 2007 and the 'cliff-edge'

People who reached State Pension Age before 6 April 2010 still needed to have 39 or 44 years of National Insurance contributions to qualify for a full Basic State Pension.

This sudden drop off in qualifying years, known as the 'cliff-edge', was perceived by some stakeholders as unfair, especially to women. After much debate in Parliament, provision was introduced under the *Pensions Act 2008* to enable certain people reaching SPA between 6 April 2008 and 5 April 2015 to buy an additional 6 years of voluntary Class 3 NICs for tax years after 1975/76.[10]

Example[11]

After 6 years of full-time education Mary starts work on her 22nd birthday. She works for 4 years then takes an 18-year break to care for her only child, before recommencing employment and working for 16 years until her SPA.

Mary works for a total of 20 years, giving her 20 qualifying years (since no credit is ever given for contributions made in the tax year in which an individual reaches SPA).

Since childcare credit only applies while the child is below age 12, Mary receives 12 years of credit. In addition, she will have been credited with minimum contributions for the tax years in which she was 16, 17 and 18 and in full time education (although she was in full time education for 6 years, the maximum credit for full time education is 3 years).

Mary has 35 years of credits (20 years of work + 3 years of full time education + 12 years of childcare credit) and is therefore eligible for a full BSP since the number of qualifying years required for a full BSP is 30. This amounts to £107.45 in 2012/13.

[8] Assuming no Home Responsibilities Protection is awarded
[9] Although most recipients are women, HRP is unisex - it is available to the person to whom child benefit is payable
[10] www.parliament.uk/briefingpapers/commons/lib/research/briefings/snbt-03111.pdf
[11] Throughout this paper, examples relate to entitlement under current rules in the pension system. Changes outlined in the Pensions Act could alter individuals' future entitlements.

Had there been no childcare credit Mary would have received only 77% (23/30) of BSP, or £82.38 per week.

This example assumes Mary reaches state pension age after 6 April 2010, when the relevant changes in the Pensions Act 2007 come into effect.

If Mary had retired before 6 April 2010 then she would have received a pension of 96% (23/24) of the full BSP (20 years of work + 3 years of full time education, 39 years requirement – 15 HRP years for childcare). This is: £107.45 x 23/24 = £102.97.

Married couples

If both husband and wife have a satisfactory NI contribution record then they will each receive a full BSP when they reach SPA. However, if the wife is entitled to less than 60% of the full BSP and she is over state pension age, she may be 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.

Prior to April 2010, if the wife was under state pension age and the husband was over state pension age and claiming the BSP, then the husband could have been eligible for an adult dependency increase to his state pension in respect of the wife, equal to 60% of the full BSP.

Women and SPa

Table 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 1: Comparing the effects of Pensions Act 1995 and Pensions Act 2011 provisions on womens' SPa

	Pension Act 1995		Pension Act 2011	
Date of birth	**State Pension Date**	**State Pension Age**	**State Pension Date**	**State Pension Age**
6 Apr 1950 - 5 May 1950	6 May 2010	60 yrs 1mths - 60 yrs 0mths		
6 May 1950 - 5 Jun 1950	6 Jul 2010	60 yrs 2mths - 60 yrs 1mths		
6 Jun 1950 - 5 Jul 1950	6 Sep 2010	60 yrs 3mths - 60 yrs 2mths		
6 Jul 1950 - 5 Aug 1950	6 Nov 2010	60 yrs 4mths - 60 yrs 3mths		
6 Aug 1950 - 5 Sep 1950	6 Jan 2011	60 yrs 5mths - 60 yrs 4mths		
6 Sep 1950 - 5 Oct 1950	6 Mar 2011	60 yrs 6mths - 60 yrs 5mths		

6 Oct 1950 - 5 Nov 1950	6 May 2011	60 yrs 7mths - 60 yrs 6mths		
6 Nov 1950 - 5 Dec 1950	6 Jul 2011	60 yrs 8mths - 60 yrs 7mths		
6 Dec 1950 - 5 Jan 1951	6 Sep 2011	60 yrs 9mths - 60 yrs 8mths		
6 Jan 1951 - 5 Feb 1951	6 Nov 2011	60 yrs 10mths - 60 yrs 9mths		
6 Feb 1951 - 5 Mar 1951	6 Jan 2012	60 yrs 11mths - 60 yrs 10mths		
6 Mar 1951 - 5 Apr 1951	6 Mar 2012	61 yrs 0mths - 60 yrs 11mths		
6 Apr 1951 - 5 May 1951	6 May 2012	61 yrs 1mths - 61 yrs 0mths		
6 May 1951 - 5 Jun 1951	6 Jul 2012	61 yrs 2mths - 61 yrs 1mths		
6 Jun 1951 - 5 Jul 1951	6 Sep 2012	61 yrs 3mths - 61 yrs 2mths		
6 Jul 1951 - 5 Aug 1951	6 Nov 2012	61 yrs 4mths - 61 yrs 3mths		
6 Aug 1951 - 5 Sep 1951	6 Jan 2013	61 yrs 5mths - 61 yrs 4mths		
6 Sep 1951 - 5 Oct 1951	6 Mar 2013	61 yrs 6mths - 61 yrs 5mths		
6 Oct 1951 - 5 Nov 1951	6 May 2013	61 yrs 7mths - 61 yrs 6mths		
6 Nov 1951 - 5 Dec 1951	6 Jul 2013	61 yrs 8mths - 61 yrs 7mths		
6 Dec 1951 - 5 Jan 1952	6 Sep 2013	61 yrs 9mths - 61 yrs 8mths		
6 Jan 1952 - 5 Feb 1952	6 Nov 2013	61 yrs 10mths - 61 yrs 9mths		
6 Feb 1952 - 5 Mar 1952	6 Jan 2014	61 yrs 11mths - 61 yrs 10mths		
6 Mar 1952 - 5 Apr 1952	6 Mar 2014	62 yrs 0mths - 61 yrs 11mths		
6 Apr 1952 - 5 May 1952	6 May 2014	62 yrs 1mths - 62 yrs 0mths		
6 May 1952 - 5 Jun 1952	6 Jul 2014	62 yrs 2mths - 62 yrs 1mths		
6 Jun 1952 - 5 Jul 1952	6 Sep 2014	62 yrs 3mths - 62 yrs 2mths		
6 Jul 1952 - 5 Aug 1952	6 Nov 2014	62 yrs 4mths - 62 yrs 3mths		
6 Aug 1952 - 5 Sep 1952	6 Jan 2015	62 yrs 5mths - 62 yrs 4mths		

6 Sep 1952 - 5 Oct 1952	6 Mar 2015	62 yrs 6mths - 62 yrs 5mths		
6 Oct 1952 - 5 Nov 1952	6 May 2015	62 yrs 7mths - 62 yrs 6mths		
6 Nov 1952 - 5 Dec 1952	6 Jul 2015	62 yrs 8mths - 62 yrs 7mths		
6 Dec 1952 - 5 Jan 1953	6 Sep 2015	62 yrs 9mths - 62 yrs 8mths		
6 Jan 1953 - 5 Feb 1953	6 Nov 2015	62 yrs 10mths - 62 yrs 9mths		
6 Feb 1953 - 5 Mar 1953	6 Jan 2016	62 yrs 11mths - 62 yrs 10mths		
6 Mar 1953 - 5 Apr 1953	6 Mar 2016	63 yrs 0mths - 62 yrs 11mths		
6 Apr 1953 - 5 May 1953	6 May 2016	63 yrs 1mths - 63 yrs 0mths	6 Jul 2016	63 yrs 3 mths - 63 yrs 2 mths
6 May 1953 - 5 Jun 1953	6 Jul 2016	63 yrs 2mths - 63 yrs 1mths	6 Nov 2016	63 yrs 6 mths - 63 yrs 5 mths
6 Jun 1953 - 5 Jul 1953	6 Sep 2016	63 yrs 3mths - 63 yrs 2mths	6 Mar 2017	63 yrs 9 mths - 63 yrs 8 mths
6 Jul 1953 - 5 Aug 1953	6 Nov 2016	63 yrs 4mths - 63 yrs 3mths	6 Jul 2017	64 yrs 0 mths - 63 yrs 11 mths
6 Aug 1953 - 5 Sep 1953	6 Jan 2017	63 yrs 5mths - 63 yrs 4mths	6 Nov 2017	64 yrs 3 mths - 64 yrs 2 mths
6 Sep 1953 - 5 Oct 1953	6 Mar 2017	63 yrs 6mths - 63 yrs 5mths	6 Mar 2018	64 yrs 6 mths - 64 yrs 5 mths
6 Oct 1953 - 5 Nov 1953	6 May 2017	63 yrs 7mths - 63 yrs 6mths	6 Jul 2018	64 yrs 9 mths - 64 yrs 8 mths
6 Nov 1953 - 5 Dec 1953	6 Jul 2017	63 yrs 8mths - 63 yrs 7mths	6 Nov 2018	65 yrs 0 mths - 64 yrs 11 mths
6 Dec 1953 - 5 Jan 1954	6 Sep 2017	63 yrs 9mths - 63 yrs 8mths	6 Mar 2019	65 yrs 3 mths - 65 yrs 2 mths
6 Jan 1954 - 5 Feb 1954	6 Nov 2017	63 yrs 10mths - 63 yrs 9mths	6 May 2019	65 yrs 4 mths - 65 yrs 3 mths
6 Feb 1954 - 5 Mar 1954	6 Jan 2018	63 yrs 11mths - 63 yrs 10mths	6 Jul 2019	65 yrs 5 mths - 65 yrs 4 mths

6 Mar 1954 - 5 Apr 1954	6 Mar 2018	64 yrs 0mths - 63 yrs 11mths	6 Sep 2019	65 yrs 6 mths - 65 yrs 5 mths
6 Apr 1954 - 5 May 1954	6 May 2018	64 yrs 1mths - 64 yrs 0mths	6 Nov 2019	65 yrs 7 mths - 65 yrs 6 mths
6 May 1954 - 5 Jun 1954	6 Jul 2018	64 yrs 2mths - 64 yrs 1mths	6 Jan 2020	65 yrs 8 mths - 65 yrs 7 mths
6 Jun 1954 - 5 Jul 1954	6 Sep 2018	64 yrs 3mths - 64 yrs 2mths	6 Mar 2020	65 yrs 9 mths - 65 yrs 8 mths
6 Jul 1954 - 5 Aug 1954	6 Nov 2018	64 yrs 4mths - 64 yrs 3mths	6 May 2020	65 yrs 10 mths - 65 yrs 9 mths
6 Aug 1954 - 5 Sep 1954	6 Jan 2019	64 yrs 5mths - 64 yrs 4mths	6 Jul 2020	65 yrs 11 mths - 65 yrs 10 mths
6 Sep 1954 - 5 Oct 1954	6 Mar 2019	64 yrs 6mths - 64 yrs 5mths	6 Sep 2020	66 yrs 0 mths - 65 yrs 11 mths
6 Oct 1954 - 5 Nov 1954	6 May 2019	64 yrs 7mths - 64 yrs 6mths	66th birthday	66 yrs

First tier: Deferral of state pensions

Individuals can choose to defer[12] the commencement of their BSP in return for an enhanced pension, through the award of increments, or as a one-off lump sum.[13]

Until April 2005, the basis for determining increments was that each pension would be increased by 1% for each 7 weeks of deferral. From April 2005, the terms have been improved so the pension is increased by 1% for each 5 weeks of deferral. Until April 2005, state pension could not be deferred past age 70. From April 2005, this restriction has been removed.

For each 5 weeks of deferral, people can receive an increase of 1% in their pension. This is equivalent to an increase of around 10.4% for each year people defer. Increments can be earned after payments have started if recipients request that the Department for Work and Pensions cease payments. Increments will be earned at the same rate.

Similar rules are in place for other state pensions including the Graduated Retirement Benefit, SERPS and S2P. However, individuals must defer all state pension benefits – they cannot elect for instance to defer BSP but start receiving SERPS.

While benefit is being deferred, the amount not claimed is still counted as income for Pension Credit and other means-tested benefits.

Benefit that has been deferred for 12 consecutive months from April 2005 can be taken as a one-off lump sum payment, rather than as an increase in future pension payments. The deferred benefit will accrue interest at 2% above the Bank of England Base Interest Rate, and the whole of the resulting lump sum will be taxable at the marginal rate of tax paid by the pensioner on his or her other income.[14] Because of the interest rate available, there can be a financial gain from deferring and taking a lump sum. The actual gain is not the full value of the lump sum (as it can be claimed and invested instead) but the value of any extra interest over and above what could be gained from claiming the pension and investing it. If the pension could be taken and invested at a higher rate than the 2% above the Bank of England base rate, it would suggest that deferring may not be cost effective.

[12] DWP (2010) *State Pension Deferral, Your Guide.* www.direct.gov.uk/prod_consum_dg/groups/dg_digitalassets/@dg/@en/@over50/documents/digitalasset/dg_180189.pdf
[13] Increments can also be awarded if payment is delayed for other reasons, such as a delay in returning the forms, or the Department for Work and Pensions not being aware of a change of address. Whatever the reason for the delay, individuals can only receive a 'back-payment' of up to 3 months of the missed payments.
[14] Even if some of the lump sum would normally have fallen in a higher tax band

Second tier: State Earnings Related Pension Scheme (SERPS)

SERPS was introduced in 1978 as a state earnings related pension scheme. It was established under the Social Security Pensions Act 1975 and replaced the Graduated Retirement Benefit (see later section in this Annex for further details on GRB).

SERPS was originally scheduled to provide a pension of 25% of band earnings – annual earnings up to a maximum of 53 times the weekly Upper Earnings Limit (UEL), and less a deduction of 52 times the weekly Lower Earnings Limit (LEL)[15] - linking the pension payable to earnings while in employment. The pension would be higher for higher earners, but capped.

All employees were members of SERPS, and have earned SERPS pension for any periods of employment, unless they:

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

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

SERPs was funded through National Insurance contributions on a pay-as-you-go basis. Subsequent changes have reduced the amount individuals can accrue through SERPS contributions, and from 2002/3 SERPS was replaced with the State Second Pension.

SERPS is payable from SPA and is taxable. Once in payment, it increases in line with prices.

The accrual rate was 1.25% of band earnings for each of the 'best 20 years' of membership. The best 20 years acted as protection for those with fluctuating earnings, with periods of self-employment or with periods outside the labour force. Those reaching SPA prior to 1998/9 would have less than 20 years of membership, and so accrued a smaller benefit.

In the Social Security Act of 1986 measures were introduced to reduce the value of future SERPS accruals:

[15] Originally the LEL was not deducted until the year before reaching SPA. Subsequent calculation changes led to the LEL being deducted in the year of accrual. 53 times the weekly UEL is used where an individual has more than one job and is paid by more than one employer at the same time. For someone remaining in the same employment throughout the tax year, the maximum is 52 times the weekly UEL.

- The best 20 years rule was removed and replaced by lifetime revalued band earnings. This disadvantaged most those with fluctuating earnings or with an incomplete employment record.
- The accrual rate was reduced for those reaching SPA after 1998/9 – the long-term target for accrual after 1987/8 was reduced from 25% to 20% of revalued band earnings.

From 1978, members could contract-out of SERPS and into an employer's pension scheme. In addition, from 1988 instead of accruing a SERPS pension members could contract-out and receive a rebate into a personal pension instead[16].

The 1995 Pensions Act introduced a further change to the calculation method – the overall effect of which was to reduce entitlement further.

In 2002/3 SERPS was replaced with State Second Pension (S2P). There will be no impact on SERPS benefits already earned. The maximum additional state pension (from a combination of GRB, SERPS and S2P) that can be received per week by a single person is £161.94 (2012/13).[17]

Sources

Department for Work and Pensions (DWP) (2008) *A Guide to State Pensions -NP46 Section – Additional State Pension*
http://www.thepensionservice.gov.uk/pdf/np46/np46sept08.pdf
Reardon A. (2002) *Zurich Pensions Handbook*

[16] See RN Second tier: Contracting-out
[17] www.direct.gov.uk/en/Pensionsandretirementplanning/StatePension/DG_183780

Second tier: State Second Pension (S2P) accrual – comparisons with SERPS accrual

After the 1986 and 1995 reforms an employee with a full work record reaching SPA after 2008/9 could expect a SERPS pension of approximately 20% of their band earnings. State Second Pension (S2P) is designed to give lower earners a higher benefit than this.

Under SERPS the benefit accrual was based on all earnings between the Lower Earnings Limit (LEL) and the Upper Earnings Limit (UEL) whereas with S2P band-earnings were divided into 3 separate bands until 2010:

- The first band is between the LEL and the Lower Earnings Threshold (LET) (£4,940 and £13,900 from April 2009).
- The second band is between the LET and the Upper Earnings Threshold (UET) (£13,900 and £31,800).
- The third band is between the UET and the UEL (£31,900 and £43,888).

The two band-earnings for S2P from 2010 on are the following:

- The first band is between the Lower Earnings Limit (LEL) and the Low Earnings Threshold (LET) (£5,564 and £14,700 from April 2012).
- The second band is between the LET and the Upper Accrual Point (UAP) (£14,700 and £40,040).

Under SERPS, a man with a potential 49 years of membership (from age 16 to SPA at age 65), would each year accrue a pension of 20%/49 of band-earnings[18]. In comparison under S2P the accrual rate varies with the bands. So for a man with a potential total membership of SERPS and S2P of 49 years the accrual rates for S2P up until 2010 were:

- 40%/49 - for earnings in the first band
- 10%/49 - for earnings in the second band
- 20%/49 - for earnings in the third band

The accrual rates for S2P from 2010 on are:

- 40%/49 - for earnings within the first band
- 10%/49 - for earnings within the second band

In addition where earnings are below the LET, then under S2P the individual is treated as if they earned at that threshold. Qualifying carers or disabled people are also treated as if they earned at that threshold.

The UET is deliberately set such that at this point the total benefit accrual is equivalent for both SERPS and S2P i.e. 20% * (£31,800 - £4,940) ≈ 40% * (£13,900 - £4,940) + 10% * (£31,800 - £13,900)[19]. In order to enable

[18] If they spent their entire working life under the post 1986 system
[19] Exact equality does not hold due to rounding

equivalence, the second band is set as roughly twice as wide as the first band - the difference between £31,800 and £13,900 is £17,900 whereas the difference between £13,900 and £4,940 is £8,960.

Table 2: Comparison of SERPS and S2P accrual – 2009/10[20]

Earnings from employment	Band earnings	SERPS accrual[21] (p.a.)	S2P accrual (p.a.)	Gain from S2P
Carer - £0	-	-	£73	£73
£3,000	-	-	-	-
At LEL - £4,940	-	-	£73	£73
£5,1400	£200	£1	£73	£72
£10,000	£5,060	£21	£73	£52
At LET - £13,900	£8,960	£37	£73	£37
£19,000	£14,060	£57	£84	£26
£25,000	£20,060	£82	£96	£14
At UET - £31,000	£26,860	£110	£110	-
£35,000	£30,060	£123	£123	-
At UEL - £43,888	£38,948	£159	£159	-
£50,000	£38,948	£159	£159	-

Sources

Department for Work and Pensions (DWP) (2008) *A Guide to State Pensions -NP46 Section – Additional State Pension*
http://www.thepensionservice.gov.uk/pdf/np46/np46sept08.pdf
Department for Work and Pensions (DWP) (2008) *Revaluation of Earnings Factors Orders* www.dwp.gov.uk/asd/reval.asp

[20] Assumes potentially 49 years of service
[21] Annual amount

Second tier: Graduated Retirement Benefit (GRB)

The Graduated Retirement Benefit (GRB) was a compulsory scheme introduced in April 1961 through the National Insurance Act 1959. It was discontinued from April 1975.

As with all state schemes the pension is payable from SPA, although commencement can be delayed and increments earned, and is funded on a pay-as-you-go basis. Once in payment, the pension increases in line with prices[22].

Employees who were not members of an occupational pension scheme and whose weekly earnings exceeded the minimum threshold of £9.00 (in 1960's cash terms) paid graduated contributions in addition to their NI Class 1 contributions. These graduated contributions were converted into 'units' of graduated retirement pension. For men, each £7.50 of graduated contributions purchased one unit of graduated retirement pension whereas for women each £9.00 purchased one unit. From 2010 the terms of conversion will be equalised at £7.50 per unit purchased – this coincides with the commencement of the changes to the SPA for women.

The maximum number of units that could be purchased was 86 for a man and 72 for a woman – equivalent to total contributions of £645 and £648 respectively. A full-time manual male employee on average weekly earnings - £15.07 in 1961 rising to £55.70 in 1975 - would, by 1975, have paid approximately 83%[23] of the maximum.

Those who had paid sufficient contributions to secure the maximum pension ceased paying graduated contributions. This limited the tax raising capability of the scheme. By 1975 many people had reached – or were close to reaching - maximum benefits.

The pension is taxable as earned income and a 50% widow(er)'s pension is automatically provided. For example, the maximum weekly benefit amount from GRB payable to a man retiring 2012/13 is £10.76.[24]

A man on average earnings[25] and making graduated contributions between 1961 and 1975 would, if retired, receive a graduated retirement pension of approximately £8.42 per week. The equivalent figure for a

[22] Indexation was introduced in 1978
[23] PPI calculation
[24] Excluding any increments for delayed commencement, and assuming that the maximum number of 86 GRB units are accrued.
[25]Average earnings for a full-time manual male employee between 1961 and 1975

woman, employed throughout the same period, and on average earnings for a full-time manual female employee is £1.96 per week.

Sources

Department for Work and Pensions (DWP) (2008) *A Guide to State Pensions -NP46 Section - Increases payable with your state pension - Graduated Retirement Benefit* http://www.thepensionservice.gov.uk/pdf/np46/np46sept08.pdf
Department for Work and Pensions (DWP) (2008) *Abstract of Statistics 2007 Section 5 - Rates of Benefit* www.dwp.gov.uk/asd/asd1/abstract/Abstract2007.pdf
Department for Work and Pensions (DWP) (2007) DWP Tabulation Tool www.dwp.gov.uk/asd/tabtool.asp

Second tier: Accessing pension savings pre-Freedom and Choice

Until June 2010, individuals with Defined Contribution (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.

Prior to April 2015 individuals could buy:

- Capped Drawdown –Investing pension savings in an income drawdown arrangement with no upper age limit and with a withdrawal cap of 150% (from March 2014) of what they would have received from an equivalent annuity.
- Flexible drawdown/Flexi access income drawdown – Individuals could withdraw unlimited amounts from their pension savings, provided that they can demonstrate that they have a secure income already in payment, guaranteed for life of £12,000 a year from 2011.

Third tier: Preserved rights and protection

The Social Security Act 1973 first introduced protection for those leaving occupational pension schemes before retirement, or early leavers. Prior to then many schemes provided nothing for the job mover. Since then, a number of further provisions have been made to increase the rights of early leavers.

Individuals have to be a member for at least 2 years before they are statutorily entitled to full 'vested' or preserved pension benefits. This is known as the vesting period.

The options available for an individual who leaves employment after the vesting period and with preserved benefits are:
- to leave the deferred pension within the original scheme, or
- to take a transfer value i.e. cash equivalent of the individual member's rights into an individual arrangement such as a personal pension, or
- to take a transfer value to the new employer's pension scheme.

The Pensions Act 2004 introduced new rights for employees who leave after 3 months but before the end of the vesting period. Since April 2006, these employees have two options of:
- a refund of their own contributions, or
- a cash transfer sum to take to another scheme.

If a member leaves a scheme with less than 3 months service – and so is not eligible for a preserved benefit - they will receive a refund of their own contributions, but not any made by the employer.[26]

Some pension schemes automatically provide an entitlement to full preserved pension benefits, irrespective of how long the person is a member of the scheme.

[26] This was reduced from 2 years by the 2004 Pensions Act

Acknowledgements and contact details

This document is the historical annex to the Pensions Primer, which 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 Reference Notes.

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Contact: Chris Curry, PPI Director

Telephone: 020 7848 3731
Email: chris@pensionspolicyinstitute.org.uk

Pensions Policy Institute
King's College London
3rd Floor, Room 311
26 Drury Lane
London WC2B 5RL

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