PENSIONS POLICY INSTITUTE
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"Pension reform sooner rather than later" says Pensions Policy Institute

Pension reform should be done sooner rather than later, says the Pensions Policy Institute today. In the latest in their series on state pension reform, the independent research organisation shows the complexity of unwinding the current means-testing policy.

"There is a huge consensus for reform of the state pension system so that means-testing can be drastically reduced", said PPI Director Alison O'Connell.

"But instead, means-testing is spreading fast, and the Savings Credit part of Pension Credit is especially complicated. The number of people eligible for Savings Credit only will increase by two-thirds over the next ten years, and most people will be eligible for Pension Credit at some stage of their retirement.

It is almost unanimously agreed that reform will be good for the people of the UK and delaying it will only make the task harder."

The paper examines the short-term effects of different reform options. Many organisations and pension experts favour simplifying the system to one state pension, either by increasing the Basic State Pension or by changing to a Citizen's Pension.

Both methods should leave no pensioner worse off, and many pensioners who do not claim their entitlement to Pension Credit will gain.

As the current system leads to a wide range of pensioner incomes, detailed analysis of what would happen to different individuals' incomes under any reform is critical. The PPI report shows that increasing the Basic State Pension could lead to windfall gains for richer pensioners, who already do well out of the system. The Citizen's Pension focuses on the poorest pensioners, so better protects those who tend to be under-pensioned.

"There has been a good deal of debate about the right system for the long-term", said Alison O'Connell. "But even if reform would make sense for tomorrow's pensioners, today's pensioners also have to be convinced.

Working out how transition to a new pension system would affect people in different circumstances is not easy as the current system is so complicated. But it is important we keep moving the reform debate on".

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Notes For Editors –
Some notes on Pension Credit are attached as background information.

A short summary of the report's main conclusions are also attached. The full report, *State Pension Reform: Managing Transition* can be found on the PPI's website: www.pensionspolicyinstitute.org.uk.

Copies can also be obtained from the PPI on 020 7848 3744 or info@pensionspolicyinstitute.org.uk

The PPI is an independent research organisation, focused on pension provision. Its aim is to improve information and understanding about pensions (state and private) through research and analysis, discussion and publication.

Managing Transition: Summary of conclusions

Insofar as current and new pensioners will be affected by transitioning to a new pension system:

1. Transition to any new pension policy has been made more complex by the Pension Credit, specifically the Savings Credit element. This means that:
   - What to do with Savings Credit will be an important part of any transition plan.
   - As Savings Credit awards are increasing fast, reform will be easier to do sooner rather than later.

2. The choice between increasing the Basic State Pension or moving to a Citizen's Pension depends in part on the decision on whether the new state pension should be paid in addition to accrued state pension entitlement or should be offset.
   - The addition method will be more regressive, giving windfall gains to richer pensioners.
   - The offset method will be more progressive, improving income immediately for poorer pensioners.

   The logic of this choice is consistent with the choice between **contributory or citizenship** as the appropriate criterion for state pension entitlement: the former tends to favour people who do well at work, the latter protects people who are under-pensioned in the current system.

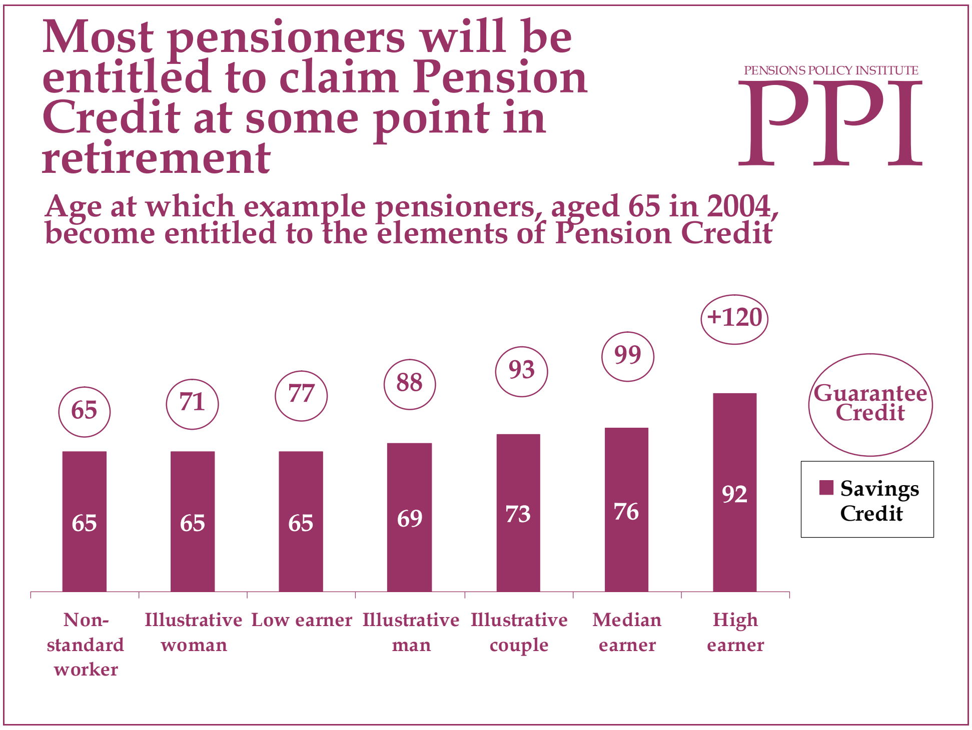
3. Policy reform options that change the rate of accrual of the existing pensions - for example, to make State Second Pension more generous - avoid transition issues but will not improve pensioner incomes in the short-term.

In practice, the choice of a new pension system, and the transition path, will be about making trade-offs between the potential 'winners and losers'. Given the complexity and range of outcomes possible from the current system, it is important to identify the real effects of reform.

Some notes on Pension Credit for pensioners
The means-tested benefit **Pension Credit** is made up of two components: **Guarantee Credit** tops up income to at least £105.45 per week (single) or £160.95 per week (couple). **Savings Credit** can give up to £15 p.w. more to eligible single claimants, or up to £20 p.w. to couples.

There are currently fewer than 1 million households eligible for Guarantee Credit only; 1.4m eligible for both Guarantee Credit and Savings Credit; and 1.2m eligible for Savings Credit alone. Over the next 10 years, the number eligible for Guarantee Credit is expected to fall slightly; the number entitled to both components to increase by one-third; and the number entitled to Savings Credit only to increase by two-thirds.

Even if people are not eligible for Pension Credit immediately they retire, as they get older the value of their pension income declines relative to the means-testing level, and they are likely to become eligible, first to Savings Credit, then to Guarantee Credit. The chart below shows some examples of this with profiles of typical pensioners.



For example, a typical single woman is eligible for the Savings Credit component of Pension Credit at age 65, and becomes eligible for Guarantee Credit as well at 71. A typical couple is not eligible for Pension Credit at all until age 73 when they become entitled for Savings Credit.

The take up rate for Pension Credit is currently around 70% which means that 30% of those eligible are not receiving their entitlement.