Pensions Policy Institute Seminar: *A Stocktake on State Pension Reform*
25 November 2004

55 people attended the seminar, which was chaired by Tom Ross (Aon Consulting and Chairman, PPI).

Alison O'Connell (Director, PPI) summarised where we are on state pension reform: the current consensus and areas of disagreement.

Michelle Lewis (Pensions Officer, TUC), Ian Naismith (Head of Market Development, Scottish Widows) and Mervyn Kohler (Head of Public Affairs, Help the Aged) summarised the perspectives of their organisations.

Trevor Huddleston (Head of the Pensions Commission Secretariat and Analytical Team) outlined some relevant points from the First Report of the Pensions Commission.

The following points were raised in discussion:

1. One area for further research is whether state pensions should be set for individuals or households. For example, a single person receiving a flat-rate pension of £105 a week could be at the minimum income level, but if both partners in a couple received a full entitlement of £105 a week, they could be considerably above the current minimum acceptable income level (£160). This has an impact when circumstances change – for example there could be big fall in household income when one partner dies.

2. Even with a high flat-rate pension, means-testing will still exist in Housing Benefit and Council Tax Benefit, though the number receiving these benefits and the amounts receive should be lower. There would still be some people on Guarantee Credit. For example, under a contributory system, people without a full entitlement could receive Guarantee Credit. Fewer people should be entitled to Guarantee Credit under a Citizen's Pension, though some people who do not meet the residency criteria may still qualify.

3. It may be that the current problem of older, poorer pensioners is temporary. People buying annuities today prefer to buy level annuities, accepting a higher income initially (when they are active enough to enjoy it) and a relatively lower income at older ages. So there may not be a clear rationale for concentrating resources on the oldest pensioners.

4. A long-term consensus needs a system that cannot be tinkered with. National Insurance might provide a way of building up rights to a pension that cannot be taken away, although this does not guarantee future value. Alternatively, a simple, transparent system might prove harder to change than the current system, as any changes to benefits would be more obvious.

5. It is difficult to see Pension Credit still being around in 20 years time. However, as no alternative or transition is in place, it is not possible for advisers to assume the system will not be in place for people in their 40s and 50s today.

6. Although nearly all proposals for reform want simplification, every recent Government proposal has added complexity. This could be because people making proposals only consider their own priorities, but Government has been trying to meet all priorities. It may be better to agree which are the most important common priorities (such as simplicity) to meet.

7. It is not always clear who should be 'excluded' from a contributory system. Many proposals for a contributory system include extensions to include more people. A Citizen's Pension could be simply designed to exclude some (for example the New Zealand system excludes prisoners), whereas the contributory system becomes more complex in order to include people. The Guarantee Credit, which pays more than most people qualify for under the current contributory system, excludes very few people.

8. The level of foundation pension is a separate issue from whether it should be contributory or residency based. It is not clear if the priority should be to increase the level of the foundation pension, or increase the coverage. The costs of doing both would be higher than spending on pensions today, but could be within the funnel of doubt surrounding the future costs of the current system.

9. The UK had a flat rate pension system, with no mandatory second pension until 1978, but there were issues with inadequacy (the basic pension was low) and inequality (people with higher incomes had better access to occupational pensions).

10. In any re-design of the state pension system there should be a comprehension test (how many people would understand what they would get?) and a self-adjustment test (could the system automatically correct to long-term changes? For example, linking benefit levels to life expectancy, as in Sweden). The ability of any system to adapt to change will be important, as the world will not stand still.

11. More consideration needs to be given to the interaction between pensions, retirement and working. There should be more emphasis on 'down-shifting', for example from working 5 days to 3 days. The pensions system should encourage rather than penalise flexible retirement.

12. The uncertainty surrounding the long term future of state pensions is holding back sensible design of workplace pensions. A large problem for workplace pensions is affordability, and in particular the age at which pensions become payable. The right question is what the appropriate age should be in 20 years time, rather than what is right for today, as the age of eligibility to pension should only change after a long notice period.

13. Although the demographic changes at the aggregate level present a strong case for increasing pension ages, it is difficult to translate this into how it would affect individuals. Some groups would be affected more than others.