

**The Actuarial Profession**  
making financial sense of the future

**Pensions, benefits and social security colloquium 2011**  
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## Public Pension Policy

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### Public Pension Policy in the UK Sustainable Retirement Incomes

#### Public policy on state pensions

- Further state pension reform has been proposed in the UK
- The reforms are 'cost neutral'
- But the reforms are redistributive in a number of ways

#### Public policy on private pension saving

- Auto-enrolment is being introduced to the UK from 2012
- The long-term impacts are uncertain
- How are the two policy areas linked?
- What might the combined impact be?

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## State pension reform

### Further state pension reform has been proposed

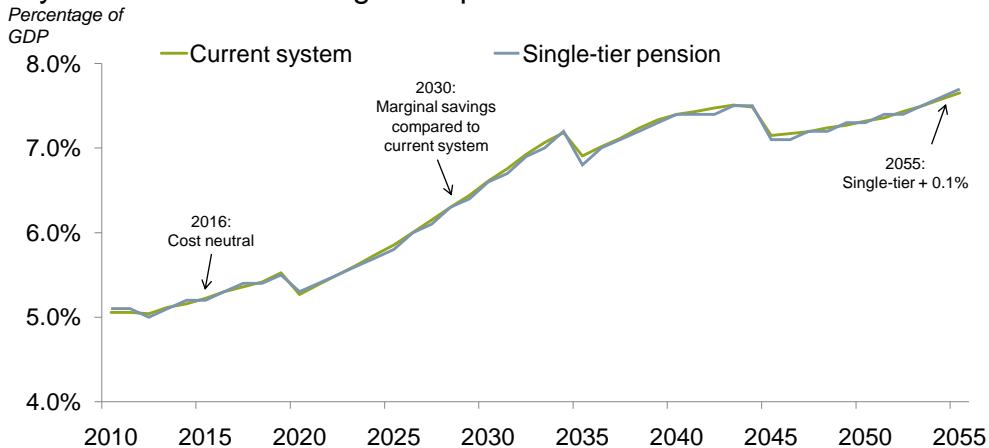
- The creation of a single-tier flat-rate pension
- Contributory – not universal
- Set above the current level of basic means testing (for example £140 per week in 2010 earnings terms)
- Uprated in-line with the 'triple-lock' index
- Abolishing second-tier pensions (and contracting-out)
- Introduced for pensioners retiring after the implementation date (for example 2016)
- Any previous rights above the new level would be protected

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## A single-tier pension could be broadly cost neutral

Projected Government spending on state pensions and Pension Credit, Housing Benefit and Council Tax Benefit under the current system and under a single-tier pension



## There would be gainers and losers from a single tier pension

### Who would gain?

- People with low entitlement to state second tier pensions – women and carers, self-employed, unemployed
- Pensioners who fail to claim means-tested benefits
- Older pensioners

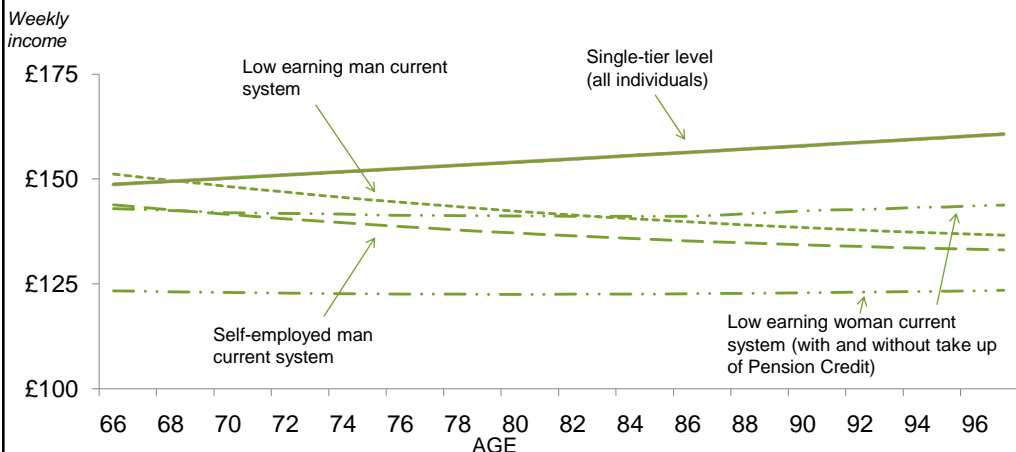
### Who would lose?

- Individuals who would have accrued higher second tier state pensions in the current system
- Some people who would have been entitled to the Savings Credit
- Those with less than 7 years of National Insurance Contributions

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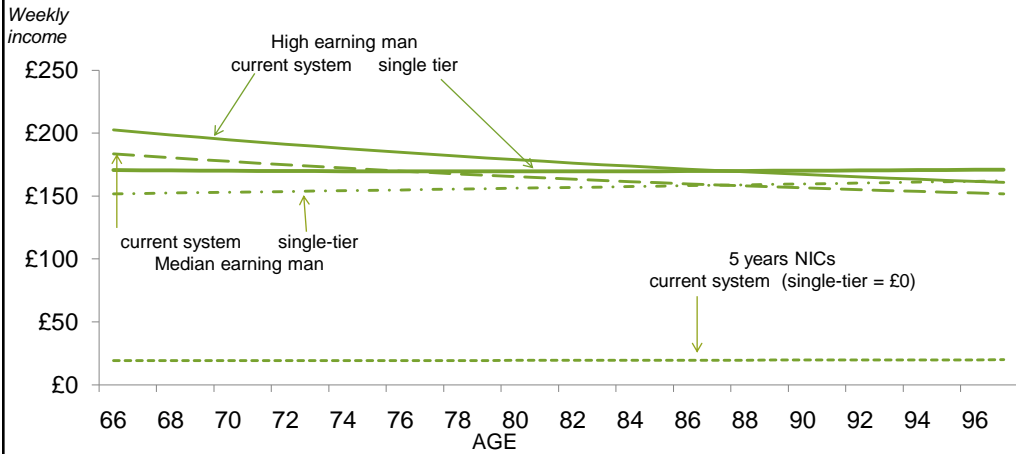
## Modelled low earners and the self-employed have better state pensions under a single-tier

Weekly state pension income for 3 hypothetical individuals, retiring at SPA in 2034 under the current system and a single-tier pension, 2011 earnings terms



## Higher earners do less well from a single-tier pension

Weekly state pension income for 3 hypothetical individuals, retiring at SPA in 2034 under the current system and a single-tier pension, 2011 earnings terms



## There would be gainers and losers from a single tier pension

2034	Couples	Singles	Total pensioners
<b>number of pensioners who gain</b>	2.4 million pensioner couples	2 million single pensioners	6.8 million pensioners
<b>average gain</b>	£28 a week (2011 earnings terms)	£11 a week (2011 earnings terms)	£23 a week (2011 earnings terms)
<b>number of pensioners who lose</b>	1.1 million pensioner couples	3 million single pensioners	5.2 million pensioners
<b>average loss</b>	- £24 a week (2011 earnings terms)	- £15 a week (2011 earnings terms)	- £18 a week (2011 earnings terms)

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## **A single-tier state pension would have wider impacts on pension provision**

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### **Transition would be complex and take a long time**

### **There would be implications for Defined Benefit schemes**

- Employers with DB schemes would pay higher National Insurance contributions
- This could lead to scheme reforms
- Employees in DB schemes would pay higher National Insurance contributions

### **There could be implications for auto-enrolment**

- Two of the aims of a single-tier pension are:
  - To reduce means-testing
  - To make the system more simple
- If this is achieved, will auto-enrolment be more successful? 8

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## **2012 Private Pension Reform: the introduction of auto-enrolment**

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### **Auto-enrolment will be introduced from 2012**

- For all individuals in work aged between 22 and state pension age, and earning above £7,475
- 4% employee contribution, 'compulsory' 3% employer contribution and tax relief, on earnings between £5,715 - £38,185
- Low cost National Employment Savings Trust (NEST) available for those whose employer does not have a qualifying pension scheme
- Auto-enrolment staged between 2012 and 2016
- Contributions phased in between 2012 and 2017

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## Auto-enrolment: How many new savers will there be?

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### Opt-out levels are uncertain

- The Government estimates that around 20% of those enrolled might opt-out – a single-tier may help this
- This is based on survey evidence
- It is broadly in line with some international evidence, but is not directly comparable:
  - In US evidence auto-enrolment is at the firm, not national, level
  - In New Zealand, auto-enrolment conditions are very different, as only new joiners are auto-enrolled

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## Employer reactions to auto-enrolment are important as well

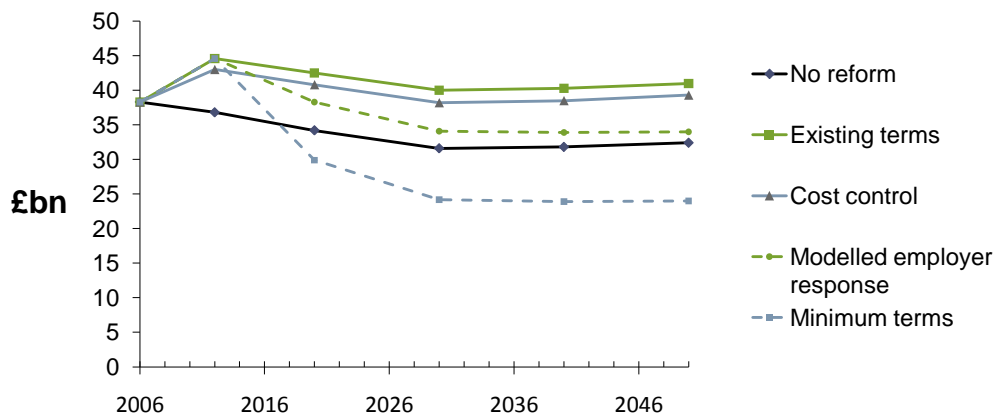
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### It is not clear how employers will react to higher costs

- The compulsory employer contribution will increase costs. In response employers may:
  - Increase prices
  - Reduce wages
  - Reduce profits
  - Lower pension costs of existing members

## Levels of long-term pension saving after the introduction of auto-enrolment depend on employer response

Annual total pension contributions, in £ billion, in 2006/7 earnings terms (unrounded figures)



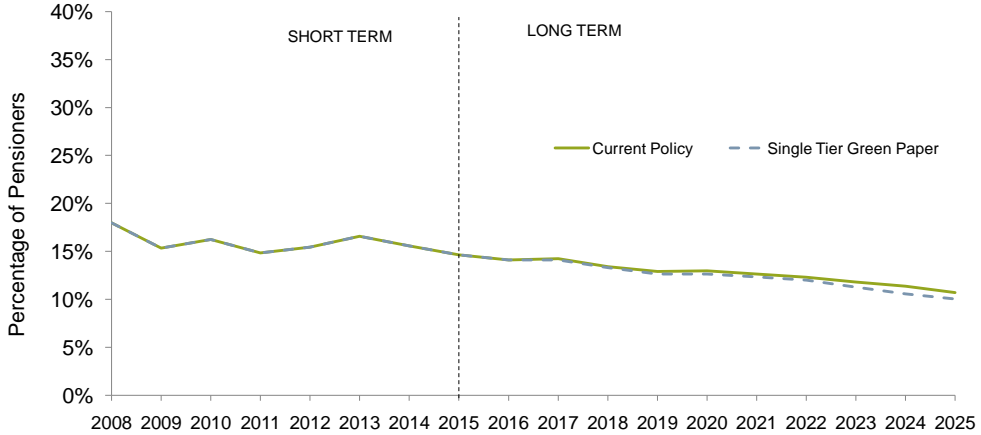
## What are the implications of the reforms for pensioner incomes?

### Both reforms are aimed at those with lower incomes

- The single-tier pension is designed to be redistributive
- It would also reduce reliance on means-testing, so remove problems with benefit take-up
- Auto-enrolment is aimed at those not currently saving.
- But there are potential losers from both policies:
  - Some receive lower state pensions under the single-tier option
  - Some employees may have lower private pensions as a result of employer responses

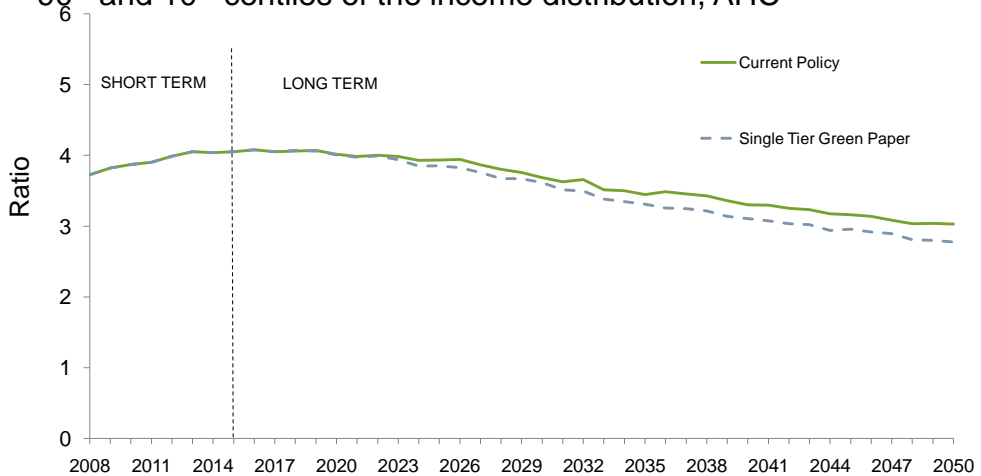
## Future relative poverty levels could reduce compared to current policy

Projected percentage of pensioners living in households with household incomes below 60% of median income, AHC



## Incomes could become more equal under the reform options

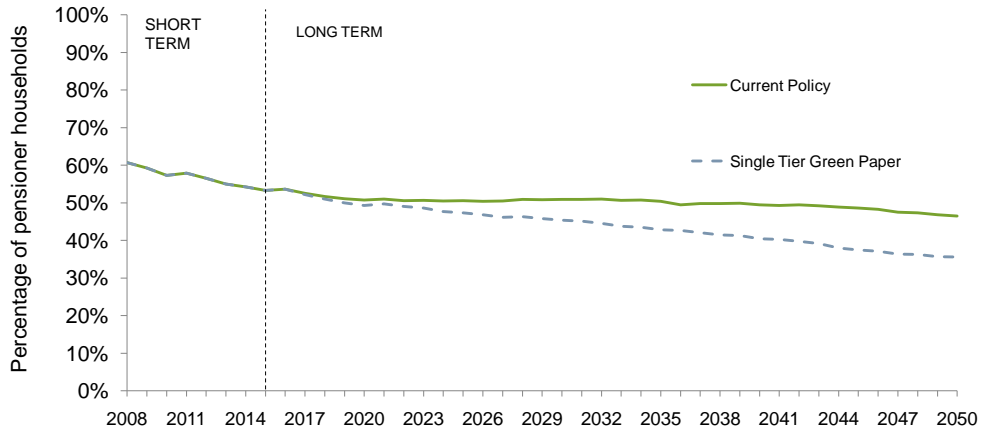
Projected ratios of pensioner households' incomes in the 90<sup>th</sup> and 10<sup>th</sup> centiles of the income distribution, AHC





## Eligibility for means-tested benefits could decline over the long term under the single-tier option

Projected percentage of all pensioner households eligible for any means-tested benefit



## Public Pension Policy in the UK Conclusions

### Conclusions

- Reform is possible without changing Government spending
- Reforms are about redistribution rather than generosity
- But they have the potential to reduce poverty and also (if simple enough!) to help auto-enrolment
- Auto-enrolment outcomes are uncertain
- More people will have private pensions
- But the overall impact on total pension saving depends on employer and employee behaviour