

# **The Pensions Bill: Social Security Aspects**

[Bill 87 of 1994/5]

**Research Paper 95/47**

**19 April 1995**



This paper outlines the provisions of the Pensions Bill that relate to social security benefits. The three areas covered are equalisation of the state retirement pension age, changes to the State Earnings Related Pension Scheme (SERPS) and war widows' pensions. These are contained in Part II of the current Bill. Two other papers are available containing details of the Bill in respect of pension fund regulation and non state benefits.

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**Summary**

This paper outlines the provisions of the Pensions Bill that relate to social security benefits. The three areas covered are equalisation of the state retirement pension age, changes to the State Earnings Related Pension Scheme (SERPS) and war widows' pensions. These are contained in Part II of the current Bill. Two other papers are available containing details of the Bill in respect of pension fund regulation and non-state benefits (occupational and personal pensions)<sup>1</sup>.

The three areas of change considered in this paper are:

- **Equalisation of the pension age.** The Bill sets in place the transition from the current state pension age for women of 60 to 65. Women currently aged 45 or over will not be affected.
- **SERPS.** The Bill changes the State Earnings Related Pension Scheme in a number of respects. Some of these changes are to allow for the rise in women's pension age. Others introduce new ways of calculating SERPS entitlement which will result in expenditure savings.
- **War widows.** Following a Government defeat in the Lords, the Bill improves the position of some war widows by allowing them a restoration of their widows' pension in the event of the failure of a second marriage.

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<sup>1</sup> Research Papers 95/46 & 95

## II Equalisation of the state pension age

### A Background

#### 1. The present system

State pension ages have been unequal for men and women since 1940. Men can draw their retirement pensions at 65, and women at 60. The same applies to the State Earnings Related Pension. It is not possible to draw either pension before this "pensionable age". People can, however, defer their pensions for up to five years and earn increments by doing this.

Retirement is no longer a precondition of receiving the full state pension at 60 or 65. Before October 1989, a person's earnings could affect the pension during the first five years after pension age. This earnings rule has now been abolished, although dependants' additions can be affected by earnings.

The full rate of state pension is £58.85 a week (April 1995-April 1996). To get this full rate it is necessary for a person to have paid or been credited with sufficient national insurance contributions for roughly nine-tenths of their "working life". Normally this means men contributing for 44 years and women for 39 years.

The amount an individual receives will often be more or less than the basic rate. People with insufficient contributions can be paid a reduced pension, providing they qualify for at least a quarter of the full rate.

There are four categories of state retirement pension:

- Category A Retirement Pension - based on a pensioner's own contributions. An increase may be paid with this for a dependent wife under pension age, or, in more limited circumstances, to a dependent husband.
- Category B Retirement Pension - based on a spouse's contributions and paid to a married woman, a widow and, in certain circumstances, a widower. In all of these cases, the recipients must be over state pension age.
- Category C Retirement Pension - a non-contributory pension paid to people who were over pension age on 5 July 1948.
- Category D Retirement Pension - a non-contributory pensions for those over 80 with no contributory pension or only a small amount.

People may also get an additional pension through SERPS (the State Earnings Related Pension Scheme). This scheme has been in place since 1978. It is built up by paying Class 1 (employees') national insurance contributions and based on a specified percentage of earnings on which national insurance contributions are paid. In the mid 1980s the Government became concerned about future costs as SERPS matured, and the 1986 Social Security Act introduced cuts to its value. Further details are given on page 24. It is possible for people in occupational and personal pension schemes to contract out of SERPS. People remain liable for contributions until they reach pensionable age. After that it is not generally possible to continue contributing.

The present system is disadvantageous for men, in that they cannot claim their pension so soon, and they have to carry on contributing for longer. The abolition of the earnings rule in 1989 allows women aged 60-65 to receive a pension even if they work, whilst retired men of these ages cannot receive one. However, there are also disadvantages for women. Although they can draw their pension at an earlier age, they cannot continue to contribute after that date. This means that if they have an incomplete record - as many women do - they have less opportunity to make this up. There are some provisions for late contributions, but the rules limit these. Women can, of course, defer their pension until 65 and earn extra increments, but as a man can defer until 70, the inequality still remains. Further discussion of the "fairness" or otherwise of the current system is provided on page 16.

## **2. The origins of unequal pension ages**

When old age pensions were first introduced under the 1908 Old Age Pensions Act, they were paid on a non-contributory basis to everyone aged 70 or over whose income fell below a certain level. Contributory pensions were introduced for 65-69 year olds in 1925. It was the 1940 Old Age and Widows Pensions Act which introduced a sex distinction in the pension age by giving women a pension at 60 but retaining 65 as the age for men.

The debates on the 1940 Bill<sup>2</sup> suggest three reasons for the change:

- there was a desire to improve pensions generally and this provided an opportunity which was less costly than other options;
- the fact that wives tended to be younger than their husbands meant that a common pension age was seen as problematic. It was felt that wives should qualify for their pensions at the same time as their husbands;
- women's domestic responsibilities on top of their paid work were felt to leave them 'tired' at 60.

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<sup>2</sup> HC Deb 20.2.40, cc. 1193-1498

### 3. Pressure for change

It has long been argued on grounds of sex equality that the state pension age should be the same for men and women<sup>3</sup>. Much debate has focused on whether it should be equalised up or down. At times of rising unemployment there tends to be pressure for a reduction in the pension age to release jobs. On the other hand, concern about falling numbers of school leavers or the increasing costs of paying state pensions tends to lead to calls for the state pension age to be raised or at least for a flexible decade of retirement.

#### 3.1 Official investigations

There have been a number of official investigations into the question of the retirement age. Details of these are provided in Library Research Notes 91/26 and 291. Three key reports were:

- the 1982 Social Services Committee Report, *Age of Retirement* which recommended a **five year flexible period of retirement** with the full pension payable at **63**<sup>4</sup>;
- the 1985 Government Green Paper which sought views on the idea of a "**retirement decade**" between **60 and 70**. In the end the matter was deferred pending further consideration<sup>5</sup>;
- the 1989 report of the House of Lords Select Committee on the European Communities.<sup>6</sup> This recommended a "**decade of retirement**" between **60 and 70** with the full pension payable at **63**.

#### 3.2 International comparisons

Many countries in the European Union and in the OECD either have equal state pension ages already or are planning to equalise them, the exceptions being Italy and Switzerland. The following table shows current and proposed pension ages in the EU and in a range of other OECD countries<sup>7</sup>:

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<sup>3</sup> See for example *Equalising the Pension Age*, Equal Opportunities Commission, 1978

<sup>4</sup> *Third Report of the Social Services Committee*, HC 26, Session 1981-82, 27.10.82

<sup>5</sup> *Reform of Social Security*, Cmnd 9518, June 1985

<sup>6</sup> *Equal Treatment for Men and Women in Pensions and Other Benefits* 10th Report of the House of Lords Select Committee on the European Communities, HL 51, Session 1988-89, 23.5.89

<sup>7</sup> Reproduced with permission of the Research Unit, Equal Opportunities Commission from *Equalisation of State Pension Ages: The Gender Impact*, Sandra Hutton, Steven Kennedy and Peter Whiteford, 1995. Original sources: *Options for Equality in State Pension Age*, DSS, Cm 1723, December 1991 and *Equality in State Pension Age*, DSS, Cm 2420, December 1993

**Table 1**

Current and proposed pension ages, European Union and other OECD countries

Country	Current Age		Planned Age	
	Male	Female	Male	Female
Belgium	Flexible between 60 and 65		No change	
Denmark	67	67	No change	
France	60	60	No change	
Germany	63	60	65	65
Greece	65	60	65 for new entrants	
Ireland	66	66	No change	
Italy	60	55	65	60
Luxembourg	65	65	Flexible from 57 to 68	
Netherlands	65	65	No change	
Portugal	65	62	65	65
Spain	65	65	No change	
<b>United Kingdom</b>	<b>65</b>	<b>60</b>	<b>65</b>	<b>65</b>
Australia	65	60	65	65
Austria	65	60	65	65
Canada	65	65	No change	
Finland	65	65	No change	
Iceland	70	70	No change	
Japan	60	56	60	60
New Zealand	60	60	65	65
Norway	67	67	No change	
Sweden	65	65	No change	
Switzerland	65	62	65	64
USA	65	65	67	67

### 3.3 Developments in European law

Moves towards sex equality in European law have also contributed to the pressure for reform. There has been a series of Directives to enforce the principle of equal treatment for men and women made under Articles 100 and 235 of the Treaty of Rome. The two main Directives in this context are as follows:

- Council Directive (EEC) 79/7 on the progressive implementation of the principle of equal treatment for men and women in matters of social security;
- Council Directive (EEC) 86/378 on the implementation of the principle of equal treatment for men and women in occupational social security schemes.

In both cases, however, there were exemptions ("derogations"), so that member states were permitted to retain unequal treatment in certain areas. State pension ages were excluded from Directive 79/7 under Article 7, so they could continue to be different for men and women.

A Draft Directive<sup>8</sup> was introduced in 1987 which was designed to close up the gaps left by the other two Directives. This is of direct relevance, as Article 9 of this would require pension ages to be equal. Transitional arrangements would protect people whose rights would be adversely affected. A number of member states, including the UK, had reservations about the draft, and an amended version was produced in 1989. In the UK, the Lords Select Committee on the European Communities considered it in detail in the report cited above (ref. 5). Concerns remained and no further action was taken until June 1991, when the European Commission re-opened consultations with member states. In a number of ways the Draft Directive has been overtaken by events.

### 3.4 Court cases

In recent years, the pressure for equalisation has increased considerably as a result of a series of cases brought before UK courts and tribunals and before the European Court of Justice (ECJ). Two key ones, the Marshall<sup>9</sup> and the Barber<sup>10</sup> cases, have involved occupational schemes rather than state pensions. The Marshall case established that men and women must have the same retirement age (as distinct from the age at which the pension can be drawn). The Barber case established that occupational pensions must be equal for men and women although it left considerable doubts about its scope which have since been the subject of a considerable number of cases<sup>11</sup>. Employers' organisations have argued that there are major practical difficulties in equalising occupational pension ages when the state pension ages are unequal. There are administrative problems caused by the fact that contracted out schemes at present have to offer a "guaranteed minimum pension" (basically a part of the pension

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<sup>8</sup> Draft Directive 9466/87; COM 87 494 Final

<sup>9</sup> Marshall v Southampton Area Health Authority 1986

<sup>10</sup> Barber v. Guardian Royal Exchange, May 1990

<sup>11</sup> For a useful summary see *Pensions Schemes and Sex Equality*, Pensions Management Institute, 1994

which is as good as that which SERPS would have provided), for which the current unequal pension age is used. There have also been uncertainties about bridging pensions paid to compensate men who retire at 60 for having to wait for their state pension.

There have been a number of cases which have tested the legality of using unequal state pension ages for other benefits, and uncertainty about these while they were pending has also increased pressure on the Government to change the law. Several hinged on the extent to which the derogation in the Equal Treatment directive<sup>12</sup> (which allows discrimination in the pension age and also in "possible consequences" for other benefits) can be relied upon to allow a number of inequalities in the UK system. In 1990, the House of Lords found against a local authority which was operating concessions for its services at 60 for women and 65 for men, establishing that the linking of age concessions to unequal pension age could only be legal if they were necessary to satisfy specific statutory requirements<sup>13</sup>. In 1992 the ECJ ruled that it is legal for men to have to pay National Insurance Contributions between the ages of 60 and 65 whereas women do not. In 1993 the European Court of Justice held that it was unlawful discrimination to deny invalid care allowance and severe disablement allowance to women aged 60 or over when those benefits would be paid to men up to the age of 65<sup>14</sup>. There is also a case pending to test whether it is legal to allow discrimination between men and women in the age up to which invalidity benefit can be paid<sup>15</sup>.

#### 4. The Consultation Document

In June 1991 the then Secretary of State for Social Security, Tony Newton announced that the Government was to address the issue of unequal state pension ages and that it would be consulting<sup>16</sup>.

In December 1991, the Government published a consultative document, *Options for Equality in State Pension Age*<sup>17</sup>. This discussed the following options.

##### Common State Pension Ages

- Equalisation at 60 for both men and women (then estimated to cost £3½bn a year by 2035)
- Equalisation at 65, with transitional provisions to allow women time to adjust (then estimated to save £3bn a year by 2035)
- Equalisation at 63 (then estimated to save around £½bn a year by 2035).

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<sup>12</sup> Article 7 (1) Council Directive (EEC) 79/7

<sup>13</sup> James v Eastleigh Borough Council, Times Law Report, 15.6.90

<sup>14</sup> Thomas and others v Chief Adjudication Officer, ECJ Case No C328/91

<sup>15</sup> The "Graham" case, CS/27/1991

<sup>16</sup> HC Deb 26.5.91 cc 998-9

<sup>17</sup> *Options for Equality in State Pension Age*, Cm 1723

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[These costings were based on 1991 prices and were revised in the subsequent White Paper - see Table 2 (page 12)]

### Flexible Schemes

- A "variable rate" scheme often canvassed as a decade of retirement, (probably between 60 and 70), with a lower pension for those retiring early and a higher one for those retiring later
- A split retirement pension scheme with SERPS payable from age 60 and the basic pension from age 65
- A contribution test scheme, where there would be a qualifying number of years' contributions required to achieve a full pension.

These flexible options were not costed in detail.

### 4.1 The responses

The consultation elicited over 4,000 responses<sup>18</sup>. Amongst those favouring equalisation at age 60 were the Equal Opportunities Commission<sup>19</sup> and the GMB union<sup>20</sup>. The TUC also argued for equalisation at 60<sup>21</sup>, as did the Campaign for Equal State Pensions<sup>22</sup>.

Organisations favouring equalisation at 65 included the Employment Institute<sup>23</sup> and the Institute of Directors<sup>24</sup>. Both of these were also attracted to a "split" arrangement with SERPS paid at a different age. The case for 65 was also argued by the Engineering Employers Federation<sup>25</sup>, and by consultants Mercer Fraser<sup>26</sup> and Towers Perrin<sup>27</sup>.

A wide range of organisations supported a flexible "decade of retirement". The crucial question here, of course, is the age at which the full pension becomes payable in such a decade - the so-called "pivotal age". It can be argued that setting this at 60 has fairly similar

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<sup>18</sup> DSS Press Release 93/14, 26.1.93.

<sup>19</sup> *A Question of Fairness*, Equal Opportunities Commission, June 1992

<sup>20</sup> *Time for Action*, GMB, 1992

<sup>21</sup> *TUC Pensions Briefing*, Number 15, September 1992

<sup>22</sup> *Response to the Government Discussion Paper*, CESP, June 1992

<sup>23</sup> *Response by Employment Institute to Options for Equality in State Pension Age*, 7 May 1992

<sup>24</sup> *Response to the Department of Social Security Consultative Document on Options for Equality in State Pension Age*, Institute of Directors, July 1992

<sup>25</sup> *Department of Social Security Discussion Document - Options for Equality in State Pension Age*, The EEF's Response, Engineering Employers Federation, 1992

<sup>26</sup> *Update: Equalising State Pension Age*, January 1992

<sup>27</sup> *Memorandum by Towers Perrin*, 1992

effects (and therefore similar costs) to choosing a fixed age of 60, as the tendency could be for people to draw their pensions as soon as possible. The Government<sup>28</sup> and others<sup>29</sup> point out that the lowest age at which the pension is payable can quickly come to be regarded as the State Pension Age. Setting it higher, however, could mean true choice only for those with sufficient alternative sources of income. Certain groups (for example people who are sick or unemployed as they approach pension age) might be forced to accept a reduced pension at 60 whilst others (particularly women with poor national insurance records) would in effect be forced to work longer for an adequate pension. Age Concern<sup>30</sup> and the National Communications Union<sup>31</sup> called for the pivotal age to be 60<sup>32</sup>. The National Association of Pension Funds<sup>33</sup> chose 63. The Confederation of British Industry<sup>34</sup>, the Association of British Insurers<sup>35</sup> and the Society of Pensions Consultants<sup>36</sup> said that it should be set at 65.

A number of organisations calling either for a fixed age of 65 or a flexible decade with the "pivotal age" at 65 argued that the resultant savings should be fed back into the system in various ways. The Institute of Directors<sup>37</sup> suggested that: "the fairest system of implementing pensions equalisation would be a combination of raising the retirement age for women but reducing the minimum number of years of contributions needed to earn a full basic pension". The Society of Pension Consultants argued that expected cost savings "should be used to increase the pensions payable in comparison with the current level of basic State pension"<sup>38</sup>. Consultants Mercer Fraser said that the savings from a common age of 65 "could give room for other State pension benefits, perhaps uprating benefits in line with earnings, albeit at a further cost"<sup>39</sup>. A useful summary of twenty-two of the major responses is provided in "Equalising State Pension Ages: Who Wants What", *Occupational Pensions*, August 1992, pp 6-9.

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<sup>28</sup> *Equality in State Pension Age*, Cm 2420, December 1993, para 1.23

<sup>29</sup> Towers Perrin, Op. Cit.

<sup>30</sup> *Age Concern England's comments on the equalisation of pension age*, Briefings, June 1992

<sup>31</sup> *Equalising State Pension Age*, National Communications Union, June 1992

<sup>32</sup> In the case of the NCU, the argument was for the pivotal age to be as "close as possible" to 60, Op. Cit. para 24

<sup>33</sup> *Options for Equality in State Pension Age Submission by the NAPF to the DSS Discussion Paper*, NAPF, June 1992

<sup>34</sup> *Options for Equality in State Pension Age - the CBI View*, CBI, 1992

<sup>35</sup> *ABI response to Government Discussion Paper: "Options for Equality in State Pension Age"*, ABI Memorandum, 29 June 1992

<sup>36</sup> *DSS Discussion Document "Options for Equality in State Pension Age": The Response of SPC*, 30 June 1992

<sup>37</sup> IOD Press Release, *Equalise state pensions at 65 - IOD*, 3 July 1992

<sup>38</sup> Op. Cit. p.1

<sup>39</sup> *Update: Equalising State Pension Age*, January 1992

### 4.2 The Social Security Advisory Committee report

The Social Security Advisory Committee (SSAC) is an independent body appointed by the Secretary of State to advise the Government on social security issues. Their main recommendation was that the pension age should be raised to 65. However, they regarded this as indivisible from other recommendations on how the savings could be spent<sup>40</sup>:

In this report we recommend equalising the state pension age at 65, using a significant part of the money saved to improve the well-being of the most vulnerable groups and, in the longer term, to make the state pension scheme of the future more responsive especially to the needs and requirements of women. This would not be achieved by preferential treatment, but by removing biases and distortions that act to reduce its value to them under present arrangements.

Equalising state pension ages at 65 and providing new safeguards for vulnerable groups by using the £3 billion which will thus become available, will introduce more flexibility. We emphasise that we regard the equalisation of pension ages at 65 over a fifteen year phasing-in period and the redeployment of the savings which will thereby accrue as an **indivisible whole**. It will be consistent with a system which is as simple and transparent as possible given the inherent complexities of the issues. Moreover, a greater proportion of the total social security budget will be spent on carefully targeted benefits than would otherwise be the case.

They summarised their proposals as follows:

#### Summary of proposals:

- state pension ages should be equalised at age 65
- implementation should be phased-in over a 15 year period beginning in 2000
- the savings derived from the change should be used to help vulnerable groups
  - the low paid particularly low-paid women
  - women returners
  - divorcees
  - carers
  - long-term sick and disabled people
  - long-term unemployed people in their mid 50's and older

#### Ways in which the £3 billion could be spent include:-

- enhancements to SERPS to assist the low paid and those with broken employment records
- a new premium with income support for those unemployed for more than 2 years and aged 55 or over and those 55 or over who are long-term sick or disabled
- enhanced home responsibility protection
- invalid care allowance to be extended to age 65 for women

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<sup>40</sup> *Options for Equality in State Pension Age: A Case for Equalising at 65*, Social Security Advisory Committee, July 1992

- Invalid Care Allowance and Severe Disablement Allowance enhanced to the contributory benefit rate
- the relationship between invalidity benefit and retirement pension should be reviewed.

## 5. The White Paper

The announcement that the Government had decided to equalise at 65 was made in the 1993 Budget statement by the Chancellor of the Exchequer, Kenneth Clarke<sup>41</sup>.

The White Paper followed soon afterwards<sup>42</sup>. This gave the following explanation for why the Government considered that unequal pension ages could be justified no longer:

### Equality

1.1 The present pension age for women was introduced in 1940. Prior to that, the state pension age was 65 for both men and women. The lower age for women was introduced largely to cope with the fact that most women were younger than their husbands and had no pensions in their own right. Much has since changed:

- women now play a full role in the workforce alongside men and most women expect to work for most of their adult lives. Women rightly expect to be treated fully on equal terms with their male colleagues (see para 1.2);
- married women are much less dependent on their husbands' National Insurance contribution records. Virtually all women will have some entitlement to a state pension in their own right by the early part of the next century (see para 1.3);
- the needs of married couples in which the husband reaches 65 ahead of his wife are now dealt with through dependency increases which did not exist when women's pension age was first reduced (see para 1.,4).

The preferential pension age for women has no place in this modern context. There is no reason for a woman to receive an earlier pension than a man if they have both paid the same contributions. The Government has therefore concluded that it is right and proper to equalise the state pension age for men and women.

The following reasons were given for choosing 65 as the common age rather than a lower one<sup>43</sup>:

- people are living longer healthier lives;
- there will be more pensioners in the next century each supported by fewer people of working age;
- public expenditure on state pensions is already set to double between now and 2025;

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<sup>41</sup> HC Deb 30.11.93 c.929

<sup>42</sup> *Equality in State Pension Age*, Cm 2420, December 1993

<sup>43</sup> *ibid.* para 1.5

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- our international competitors are facing similar pressures and are moving towards higher pension ages;
- occupational schemes are predominantly equalising at 65.

The White Paper revises the costings of equalising at different ages as follows:

**Table 2** - Exchequer costs of equalisation

Costs +ve / Savings -ve	£ billion <sup>(a)</sup>	
	2025	2035
Age 60 discussion document	4.5	3.5
Age 60 white paper	5	4
Age 63 discussion document	- 1	- 0.5
Age 63 white paper	- 1	- 0.5
Age 65 discussion document	- 3.5	- 3
Age 65 white paper	- 4	- 3

(a) Discussion document figures at 1991/2 prices; white paper figures at 1993/4 prices.

### 6. The Main Proposals

The central proposal in the White Paper was, of course, that the female pension age should be raised to 65. There would be a gradual phasing-in of the new pension age to protect older women, however. The change would not be implemented until 2010, meaning that no woman born before April 1950 would be affected. Once the process started, it would be phased in over the next 10 years, so that only women born after 6 April 1955 would have to wait for a full extra five years.

In addition to this phased increase in the female pension age, the White Paper proposed a number of improvements to state pensions:

- Family credit and disability working allowance will in future count as earnings when SERPS is calculated;
- dependency increases for a spouse, and Category B pensions based on a spouse's contributions will be equalised, so that men will enjoy the same rights as women;
- greater incentives will be given for people to defer claiming their pensions. For people who defer claiming their pension from 2010, the increments will be increased from 7½ per cent for each full year of deferment to 10 per cent.

The White Paper also made it clear that a change to Home Responsibilities Protection (HRP) already contained in legislation would be implemented as part of the package. HRP helps to protect the pension records of people who take time out of the labour market to care for children or sick or disabled people. The Social Security Act 1986 contained powers to extend HRP to cover SERPS as well as the basic pension. As the legislation to achieve this is already in place, this is not covered by the Bill.

## **B. The Bill's Provisions**

### **1. Raising women's pension ages (Clause 118(a) & Schedule 4, Part 1)**

The new rules are set out in Paragraph 1 of Schedule 4. A woman born before 6 April 1950 (currently aged 45 or over) attains pension age at 60 as now. A woman born after 5 April 1955 (currently aged 40 or under) will not attain pension age until she is 65.

Women born between these two dates will attain pension age on a series of fixed dates. They will have to wait an extra month for every month (or part month) their birthday falls after 5 April 1950.

Table 3, overleaf, shows some examples of how this will work (in practice the pension age will rise at monthly intervals, not just the six monthly ones shown in the table):

**Table 3** - Examples of new pension ages during the phasing in period\*

<b>Date of Birth</b>	<b>Pension Age</b>	<b>Date Pension Age Attained</b>
06.04.1950 - 05.05.1950	60 years 1 month	06.05 2010
06.10.1950 - 05.11.1950	60 years 7 months	06.05 2011
06.04.1951 - 05.05.1951	61 years 1 month	06.05.2012
06.10.1951 - 05.11.1951	61 years 7 months	06.05.2013
06.04.1952 - 05.05.1952	62 years 1 month	06.05.2014
06.10.1952 - 05.11.1952	62 years 7 months	06.05.2015
06.04.1953 - 05.05.1953	63 years 1 month	06.05.2016
06.10.1953 - 05.11.1953	63 years 7 months	06.05.2017
06.04.1954 - 05.05.1954	64 years 1 month	06.05.2018
06.10.1954 - 05.11.1954	64 years 7 months	06.05.2019
06.04.1955	65 year 0 month	06.04.2020

\* Schedule 4, Part I, para 1

**2. Equalising pension increases for dependent spouses  
(Clause 118(b) & Schedule 4, Part II, paras 2 & 3)**

Under the current system, where a man reaches pension age and his wife is under pension age then, subject to certain conditions, a dependency increase can be paid. This is currently £35.25 per week. When the wife reaches pension age, this is replaced by a 'Category B' pension (also £35.25) based on her husband's National Insurance record or by a 'Category A' pension based on her own record if this is better. Dependency increases and Category B pensions can also be awarded to women in respect of their husbands, but only in a much more limited range of circumstances. A woman must have been entitled to an increase in unemployment benefit or incapacity benefit for her husband just before she reached pensionable age.

Paragraph 2 of Schedule 4 equalises the conditions for increases for a spouse under pension age on the more favourable basis which currently applies to married women. It does so by removing the additional condition which currently applies only to a woman pensioner. This means that the older spouse, on reaching 65, will be able to claim a dependency increase for a younger spouse, providing the pensioner is contributing to the maintenance of the spouse and the spouse is not earning more than the increase. The new provisions apply from 2010.

Paragraph 3 equalises the conditions for Category B pensions - again, on the more favourable basis which currently applies to married women. The lower rate Category B pension available to married women will be available to married men on the same basis, and widowers' Category B pensions will be available on the same basis as those for widows. Again, the new provisions apply from 2010.

### **3. Home Responsibilities Protection**

Home Responsibilities Protection (HRP) was introduced in 1978. It helps people who care full time for children or sick or disabled people by reducing the number of years of contributions they need for a full basic State Pension. At present women can be covered for a full basic pension by HRP for up to 19 years, whilst cover for men can apply for up to 24 years.

Paragraph 4 of Schedule 4 equalises provisions for men and women. It has the effect of increasing the number of years which can be covered by HRP for women (who are the main beneficiaries) from 19 to 22 years. The same limit would apply to men - a reduction of 2 years for them.

The new provisions will apply to anyone reaching pension age after 5 April 2010.

### **4. Increments**

At present, a person can defer his or her retirement pension by up to 5 years and, in return, enhance its value by receiving increments. These are currently 1/7th per cent for each week of deferral, which is 7.4 per cent for each full year of deferral. Very few people (less than 2 per cent) actually choose to defer their pensions in this way.

Paragraph 6(3) of Schedule 4 increases the weekly increment to 1/5th per cent - which is 10.4 per cent for a full year's deferral. Paragraph 6(1) removes the age limit of 70 so that in future a person can defer their pension for as long as they like and still derive increments.

## C. Discussion

### 1. "Fairness"

Arguments concerning equal treatment of the sexes often centre on the rather elusive concept of "fairness". To some, a lower pension age for women is unfair because they enjoy the advantage without paying higher contributions. Also, as a group they enjoy a higher life expectancy, so they are likely to draw their benefit for longer even if pension ages are equal. CESPAs make this point in arguing its case for equalisation at 60:<sup>44</sup>

We believe that the existing state pension age of 65 for men is unjust, not only because it disadvantages every man against a woman of a comparable age but because statistics show that it denies all state pension to 10% of all men, the percentage who having reached age 60 do not survive to age 65. It is also a very poor return for a further 16% of men who do survive to age 65 but draw the state pension for less than 5 years.

Others - for example the Equal Opportunities Commission and the Fawcett Society<sup>45</sup> focus on ways in which the whole system of pension provision fails adequately to take account of women's employment patterns. The EOC make the following observations<sup>46</sup>:

Why do many women end up poor in their old age? Not because they are irresponsible, or have not been in employment. It is the system which fails them because it was not built with them in mind. When the present pension system was introduced, it was based on the assumption that men and women would continue to have similar family and employment roles in the future. Men would be the sole family breadwinner and most women would work only in the home and receive pension benefits via their partners. Much has changed since then, and will change again as we go into the next century. Women now make up almost half the workforce and may not rely on a partner's benefit rights given the increased incidence of divorce. Yet women still bear the main responsibility for the care of the family and this can limit their employment/earning opportunities. The ultimate effect of this different and lower paid working life is little or no pension when they reach retirement.

The Government argue that the difference in state pension ages is "the last glaring inequality in our treatment of men and women. It is outdated and unfair". They point out that women now play a "full role in the workforce" and that there is "no reason for a woman to receive an earlier pension than a man if they have both paid the same contributions"<sup>47</sup>. The Fawcett Society counter this argument as follows:

The evidence given to support this claim relates solely to the numbers of women active in the workforce. However pension entitlement is primarily linked to earnings not participation. It

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<sup>44</sup> See, for example, CESPAs Memorandum on the Pensions Bill, 1995

<sup>45</sup> *The Pensions Bill Introductory Briefing: Equal treatment in State Pensions Improving the system for Women*, Fawcett Society, February 1995

<sup>46</sup> *The Pensions Bill*, Memorandum to the Social Security Committee, Equal Opportunities Commission, 1995.

<sup>47</sup> *Ibid.* Foreword and p. 7

is not participation in the workforce that is the relevant factor, but the level of weekly or annual earnings.

Women are not playing an equal role in the workforce. Their earnings levels, which are a consequence of both rates of pay and the number of hours worked, are substantially lower than that of men (on average).

Organisations focusing on the problems women have in securing an adequate retirement income tend to argue for equalisation at 60 or, failing that, stress the need for "compensatory" measures to be made from the cost savings from equalising at 65<sup>48</sup>. Clearly the Government has made improvements to state pensions in the Bill. However, in their report for the Equal Opportunities Commission, Hutton *et al*<sup>49</sup> argue that these are not adequate:

The Government's proposals for equalisation at 65 include a number of additional measures, including counting Disability Working Allowance and Family Credit as earnings for National Insurance purposes, and the relaxation of rules enabling women to claim dependency additions in respect of their husbands. *None of these measures are likely to have much impact on women's retirement incomes.*

## 2. Costs

The consultation document makes it clear that its costings of equalising at 60, 63 and 65 are sensitive to a number of assumptions and therefore "... should not be interpreted as precise estimates but as broad indicators of the financial effects". Indeed, it provides costings using alternative assumptions<sup>50</sup>. Bryn Davies of Union Pension Services<sup>51</sup> provides radically different estimates using different assumptions to show not only that equalisation at 60 could be afforded but also that eventually it will cost the Government *more* to equalise at 65 than at 60. Part of the reason for this is that Davies assumes that if equalisation is at 60, a high proportion of those who do retire earlier as a result will be replaced in the workforce by people who are currently unemployed. He acknowledges that his figures are not necessarily more accurate than the Government's. One of the purposes of his analysis is to "indicate the full range of what is possible."<sup>52</sup>

Hutton *et al* discuss alternative costings in some detail and conclude that "... practice of quoting a single figure as the 'cost of equalisation' is, at the very least, unwise."<sup>53</sup>

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<sup>48</sup> See for example Fawcett Society, Op. Cit. p.2

<sup>49</sup> Op. Cit. (see note 6). Extract taken from summary of report attached to EOC press notice, 17.1.95

<sup>50</sup> Cm 1723, Appendix 2

<sup>51</sup> *Can we afford equality at 60?* Bryn Davies, November 1993

<sup>52</sup> Ibid, p.1

<sup>53</sup> Op. Cit. p.66

### 3. Demographic factors

The White Paper argues that demographic projections reveal a fall in the numbers of people of working age as compared to the numbers of pensioners (the "support ratio") as the post-war and 1960s 'baby booms' come to be seen in the pensioner populations:

In 1991 the ratio was 3.3 people of working age to each pensioner. This ratio is projected to fall to 2.2:1 by 2030 if pension age is unchanged. Equalising at 65 means that in 2030 the projected ratio would be 2.7:1. This is still a significant fall compared to the present day but it is more sustainable. To allow the support ratio to fall lower - for example, equalising pension age at 60 would mean a drop to 1.8:1 - would clearly be difficult to sustain.

Hutton *et al* point to the uncertainty of population projections. They also take issue with the Government's implicit assumption that the demographic support ratio is a satisfactory indicator of the 'burden' of dependency. Future patterns of growth, labour force participation and unemployment also have a crucial role. If a shrinking workforce leads to a labour shortage, unemployment would fall. Other measures besides increasing the state pension age could be taken to deal with the perceived problem of population ageing. For example, the Government could increase spending on education and training to raise the 'productivity' of the workforce and could use active labour market policies to increase the participation of married women and older people<sup>54</sup>.

### 4. International comparisons

The Government points to the fact that many countries have taken steps to raise their pension ages or have equalised at the higher level (see Table 1, page 5). To ignore this trend would place UK industry at a disadvantage<sup>55</sup>:

The situation in these countries is very similar to our own. Ignoring this trend towards higher pension ages would put our industry at a disadvantage compared to other countries. Extra costs to industry from a lower state pension age would arise in three ways. First, direct costs would be incurred through the employers' National Insurance contributions needed to finance earlier pensions. Second, there would be pressure on wage costs as a result of employees having to pay higher National Insurance than they otherwise would. Third, any moves towards earlier retirement and hence, a smaller labour force would also tend to raise wage costs and spread the tax burden over a smaller productive base. Britain's international competitiveness would suffer. Choosing a common pension age of 65 avoids these risks and keeps the UK on a par with its trading partners.

Hutton *et al* make the following criticisms of this argument<sup>56</sup>:

Public spending per person on pensions in the mid 1980s (the most recent figures available) was lower in the United Kingdom than in all other OECD countries, when expressed as a proportion of GDP. Even with the gradual maturing of SERPS, public spending per pensioner is unlikely to increase dramatically compared with other countries.

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<sup>54</sup> Ibid, p.vii

<sup>55</sup> White Paper, Op. Cit. para 1.13

<sup>56</sup> Op. Cit. p.vii

In 1980, the UK had one of the lowest support ratios (defined as the ratio of persons aged 15 to 64 to persons aged 65 and over) in the developed world. However, by 2040 only Ireland is expected to have a higher support ratio than the UK. Relative to its trading partners, therefore, the UK will be *favoured* by demographic ageing, since the demographic contribution to increased expenditure will be less in the UK than in almost all other countries.

In their responses to the 1991 consultation document, both Mercer Fraser and the Institute of Directors acknowledge the point that the UK could well be less affected than other European Union countries by the "demographic time-bomb". However, both urge against complacency. Mercer Fraser states that "comparison with our international competitors would still suggest equalisation at 65 or above"<sup>57</sup>. The IOD notes that the UK has "two huge advantages" in having rather more favourable demographic trends than most countries, and also in having curbed state pension spending already through cuts to SERPS and increasing reliance on occupational and personal schemes. Whilst it has a "breathing space", a cautious approach should be taken in determining pension ages because:

- The UK has a major competitive disadvantage in the poor quality of the education and training, and addressing this will take young people out of the workforce for longer, thus exacerbating problems with the support ratio;
- the total impact on the Exchequer of a falling support ratio and falls in the numbers of those economically active will be much worse than the consultation document said;
- there is a huge potential increase in economic and political refugees and the UK may well have to contribute to the cost of providing for them.

The IOD continues:

Prudence regarding the promises given at this stage would still leave it open for future governments to increase pensions in payment or start paying pensions earlier, if that can then be afforded when the time comes; but it is very difficult to renege on promises that people have relied on in making their own long-term financial plans, if those promises cannot be met when the time comes.

### 5. General comments on Part II of the Bill

The CBI welcomes the raising of the female pension age to 65<sup>58</sup>:

The Bill raises the pension age for women to 65. Such decisions are not easy for governments to make. All the advantages will be felt only after a generation has passed. But a decision on equality was overdue and establishing a longer career expectation for women should help in tackling the "glass ceiling" barrier to promotion and building up pension entitlement. In moving to the higher option (as opposed to 60 or 63) the UK is following the path taken by

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<sup>57</sup> Op. Cit. p.4

<sup>58</sup> *Parliamentary Brief*, CBI, 7.2.95

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other economies facing the same future cost problem such as Japan, Germany and the United States. All these countries are wealthier in GDP per head terms than the UK.

Employers welcome the Bill's provisions on equality, not least the gradual phasing in over 10 years from 2010, which means that no-one now over 45 will be affected and their plans for retirement need not be disturbed.

The Association of Consulting Actuaries<sup>59</sup> welcomes setting the age at which the full pension can be taken at 65. However, it argues for flexibility to take the pension below that age at a reduced rate:

As stated in previous evidence of the Social Security Committee we are in favour of the Government's proposals of equalising pensionable age under the State scheme at the age of 65. We would, however, wish to see greater flexibility for those individuals who take early retirement. We believe the provision of reduced pensions of equal value would have no true long term cost to the Government.

The Carnegie Third Age programme<sup>60</sup> gives a qualified welcome:

We welcome the introduction to a state pension age of 65, phased in over a period as dependency ratios worsen. We believe that employers and Government should now be looking twenty years ahead to when the baby boom generation retires, when smaller numbers of young people will be entering the labour market and when older people with updated skills are likely to be urgently needed in the labour market. At the same time the population of working age will be falling and the numbers of the retired population will be rising - with inevitable increases in the tax and contribution pressures on those at work.

However, it stresses the need for measures to ensure that the elderly have the skills and opportunities to get work, including legislation to combat age discrimination if necessary. It also stresses that savings from equalising at 65 should be used to benefit women in other ways, and expresses concern about the level of the pension.

Age Concern opposes the equalisation of the pension age at 65 and instead supports a flexible decade of retirement<sup>61</sup>:

Age Concern believes that there should be a flexible decade with a pension equal to the full basic pension available at 60 while those who continue to work and not draw their pension should gain increases. Unless a full pension is paid at the age of 60 only those with reasonable levels of private pensions or savings would be in a position to retire at this age. Others with limited private income would be forced to continue to work and effectively have little choice.

The TUC also opposes the change<sup>62</sup>:

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<sup>59</sup> *Memorandum by the Association of Consulting Actuaries to the Social Security Committee Enquiry into the operating of Pension Funds*, ACA, 1995

<sup>60</sup> *Submission to the Social Security Committee*, Carnegie Third Age Programme, 1995

<sup>61</sup> *Submission to Social Security Select Committee Review of the Pension Bill*, Age Concern, 1995

<sup>62</sup> *Pensions Bill - Briefing*, TUC, 5 January 1995

We believe the government is wrong and that each of their points can be answered. In particular they are replacing direct discrimination in pension age by indirect discrimination. Men, and in particular relatively affluent men, are far more likely to have pension arrangements that will allow them to take early retirement, therefore a pension age of 65 will lead to more women than men having to work until the state pension age.

Like the TUC, the State Pension at 60 Alliance argue that an equal state pension age at 60 can be afforded<sup>63</sup>:

The government's argument that Britain's international competitiveness would suffer if it did not increase pension ages in line with competitor countries is overstated for two main reasons. Firstly, the UK has one of the cheapest pension systems of all the OECD countries, and so spends less than almost all our trading partners. Secondly the UK is predicted to be favourably affected by demographic ageing relative to its competitor countries: by 2040, it is expected that the UK will have the second highest support ratio (working age population: pensioners) of all OECD countries.

### 6. Labour policy

Labour has supported a flexible decade of retirement between 60 and 70 for some time and has made it clear that it finds a "pivotal age" of 63 attractive, although this is subject to review in Government. The policy was set out in an article in the Independent by the Shadow Secretary of State for Social Security, Donald Dewar<sup>64</sup>:

Many will argue that the obvious way to achieve equitable treatment would be a common retirement age of 60. For an opposition party, it is tempting to give in to the pressure. But that would be irresponsible. Labour is seen as a government-in-waiting and must act like one.

Equalising at 60 would, on the Government's figures, cost £5bn in 2025. It also runs against the intuition of many people that demographic pressures require a raising of the pension age, some Tories arguing for a common age of 67.

The article goes on to explain the attractions of the "broadly neutral" pivotal age of 63:

A flexible approach would be sensible. It should be possible to draw a pension any time between 60 and 70. The idea of a decade of retirement has widespread support in the pensions industry. The Government Actuary estimates that a pivotal age - when someone with a complete contributions record receives the full state pension - could be set at 63 with a 'broadly neutral' economic impact. Indeed, it would save £1bn in real terms in 2025 and £9.5bn in 2035.

The argument points to 63 as a pivotal age, though Labour will want to review this when the technical resources of government are available to us.

If there is to be a pension age of 65, then Labour argue that savings should be used to strengthen the position of women and other disadvantaged groups.

### 7. Liberal Democrat policy

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<sup>63</sup> *Pensions Bill Briefing*, State Pension at 60 Alliance, 1995

<sup>64</sup> *Independent*, "Retiring at an age of equality" 20.2.95, p.15

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The Liberal Democrats also support a flexible period of retirement between the ages of 60 and 70. Their proposals are set out in a 1993 policy document<sup>65</sup>:

2.4.8 The demographic forecasts make it unrealistic to equalise the pension age at 60, or to make 60 the pivotal age of a decade of retirement.

2.4.9 This means that the choice is effectively between an equalisation age of 63 or 65. This is not an easy choice. Many women may be unhappy about having to work on to the age of 63 before qualifying for a full state pension, let alone until 65. But a pivotal age of 65 would make it possible for the state pension to be significantly more generous. In reaching a **final** decision on the pivotal age for the equalised state pension, Liberal Democrats recognise that:

- Setting a higher equalised pivotal age **should not be a means of taking money away from pensioners.**
- The higher the pivotal age agreed after **consultation, the higher the level of pension which should be paid when it becomes due.**

Recognising these two principles, Liberal Democrats urge the Government to consult widely and publicly before reaching a **final** decision.

Unlike Labour, they argue for a pivotal age of 65, subject to savings being fed back into the system:

2.4.15 Liberal Democrats would:

- Introduce a flexible "decade of retirement", with citizens entitled to start drawing the basic state pension at any time between the ages of 60 and 70.
- Set the same pivotal pension age for both men and women, with pensions being reduced when first drawn before that age and increased when first drawn after it.
- Phase in the equalisation of pension ages over a period of 15 years.
- Make those for whom a reduced pension starting before 65 would be inadequate for subsistence, eligible for income support, until reaching 65, when they would draw a standard pension.
- Make passport benefits currently linked to pension age available at 60.
- Give consideration to partial pension schemes.

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<sup>65</sup> *Retirement with Dignity Liberal Democrat Policies for Improving Pensioners' Quality of Life*, Federal Green Paper Number 31, September 1993

## II. State Earnings-related Pension Scheme (SERPS)

### A. Background to SERPS

The original SERPS was brought in by Barbara Castle in the Social Security Pensions Act 1975. Contributions started being made to SERPS in April 1978, and the first additional pensions were paid to people retiring in 1979. The scheme was designed to build up slowly until the first full pensions were paid in 1998/9. With the changes already made by the Social Security Act 1986, it is only people retiring in that year who will get the full planned amount. Thereafter it gets phased down. The 1986 changes were introduced as SERPS was considered too generous and the Government thought the balance between state and private provision should be altered so that people were encouraged to take out their own personal pensions rather than rely on the state scheme.

The 1986 changes were estimated to have cut the value of SERPS, in the long term, by around half.

### B. The Bill's provisions

The original Bill introduced four main areas of change to SERPS:

- As a consequence of equalising male and female pension ages, the accrual rates, revaluation of earnings factors before retirement and indexation after retirement used in the calculation of female SERPS entitlement will be aligned with those for men. This was amended as a result of a Government defeat in the Lords. (**Clause 118 -Sch 4 para 5**);
- Any Family Credit or Disability Working Allowance payments in a financial year will count towards the earnings factor used in calculating SERPS entitlements (**Clause 119**);
- The calculation of the earnings factors used to derive SERPS entitlement is to be amended. For awards of pension from 6 April 2000 onwards, the lower earnings limit in each financial year will be deducted from the relevant earnings before revaluation to retirement age. At present the lower earnings limit in the financial year before retirement is deducted from the revalued earnings factor (**Clause 120**);
- Contributors will not accrue any SERPS entitlement in respect of contracted-out earnings (**Part III Clause 128**). This change is covered in another Paper<sup>66</sup>.

#### 1. Equalisation

Schedule 4, paragraph 5 covers equalisation of female SERPS entitlement with that for men. In addition, following the Lord's consideration, a further change to SERPS is contained in the Bill to be considered by the Commons. Paragraph 5(2) is the result of a Government defeat in the Lords<sup>67</sup>. As originally introduced in the Lords, the paragraph would have left the

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<sup>66</sup> Research Paper 95/48

<sup>67</sup> Committee Stage, HL Deb 20.2.95, cc. 1001-9

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lifetime average earnings rule intact. After equalisation at 65, this would have meant 49 years for both men and women. Critics argued that this would mean reduced SERPS benefits for women unless they could find reasonably well paid employment from 60 to 64<sup>68</sup>.

When SERPS was first introduced in 1978, the benefits to be paid under it were 25 per cent of average reckonable earnings in the 20 best years of earnings - the so-called "best 20 years" rule. The Social Security Act 1986 abolished this rule so that SERPS is now calculated on reckonable earnings averaged over the whole of the working life. The working life is currently 44 years for a woman and 49 years for a man. The cuts also reduced the rate of accrual for people retiring after April 1999 from 25 per cent to 20 per cent<sup>69</sup>.

The "best 20 years" rule would eventually have allowed a woman to discard 24 lower paid years of her working life, and a man to discard 29 years.

The Opposition amendment passed by the Lords reduced the period upon which SERPS is based from the whole 49 years of the working life to the best 44 years, thus allowing both men and women to discard their 5 lowest paid years. This would represent a preservation of the current situation for women, and an improvement for men. A more ambitious amendment to reduce the period to 39 years was withdrawn. Speaking for the 44 year amendment, Labour's Baroness Hollis of Heigham argued that the change was well targeted, as it would ensure that women were no worse off than at present and that low-paid men would gain<sup>70</sup>:

The second amendment would allow the dropping of the five weakest years, thus at least ensuring that women are no worse off than at present and low paid men - those not in occupational pensions but in SERPS - would similarly benefit. Thus, the amendment benefits women and low paid men alike. It is well targeted. Without subverting the whole-life basis of SERPS, it introduces a modest flexibility; the discard of some years which the basic state-pension allows. It would permit years to be dropped at the end of the working life or, for someone in part-time work, caring for a partner, or if they are unemployed.

For the Government, Lord Mackay of Ardbrecknesh argued that the amendments would raise expenditure in a poorly targeted way because high earning men could benefit as well as low earning women. To do this would "make inroads into the steps we are taking to put SERPS on a long term sustainable basis"<sup>71</sup>:

The reforms before us ensure the continued affordability of the scheme into the future, while protecting the position of the most vulnerable groups in our country, some of which I explained. By contrast, the amendments would make inroads into the steps we are taking to put SERPS on a long-term sustainable basis. They would raise expenditure in the long term in a poorly-targeted way. Indeed, high earning men would benefit as well as low

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<sup>68</sup> Hutton, Kennedy and Whiteford, *Equalisation of State Pension Ages: the Gender Impact*, Equal Opportunities Commission, 1995, p.82

<sup>69</sup> This change is to be phased in

<sup>70</sup> HL Deb 20.2.95 c.1001

<sup>71</sup> HL Deb 20.2.95 cc. 1004-5

earning women. I cannot believe that that is what the Benches opposite seek to do. I find it hard to square their normal desire to help the poorest in the community with the way in which the amendment brings in for help some high earning men who would gain from the reduction in the number of years.

The Opposition amendment was carried by 105 votes to 61.

## **2. SERPS on family credit and disability working allowance (Clause 119)**

Family credit and disability working allowance are means-tested benefits for people with low earnings from full time work. Family credit is paid to people with children and disability working allowance is paid to people with a mental or physical disability which puts them at a disadvantage in getting a job. The effect of Clause 119 is that these benefits will be treated as if they were additional earnings when SERPS is calculated. This will apply to pension awards made from 1999 onwards. The White Paper states that for a person with the average earnings of a family credit recipient and receiving the average family credit award, the measure would increase the pension which that year's work would otherwise have earned by approximately 75%<sup>72</sup>.

## **3. Annualisation of SERPS**

**Clause 120** has two main objectives. It changes the formula for calculating the additional pension (annualisation) under SERPS for people who become entitled on or after 6 April 2000. It also removes the anomaly of class 2 (self-employed) and class 3 (non-employed) contributions producing small amounts of SERPS entitlement.

Under the current formula, SERPS is calculated by uprating past earnings by the rise in average earnings and then calculating "surplus earnings" as those which are between the lower and the upper earnings limits in the year before retirement. The formula in Clause 120 changes this to a revaluation of earnings between the two limits current in the year in which they were earned.

The earnings limits are linked statutorily to the rate of the basic Retirement Pension<sup>73</sup>. They are set by regulation, but according to the 1992 Act the lower limit has to be equal to, or no more than 99p less than, the single pension. The upper limit is prescribed as equal to seven times the basic pension, or seven times the pension plus or minus no more than half the value of the pension. In practice the lower limit is set at a whole pound figure and the upper one in multiples of five pounds.

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<sup>72</sup> Op. Cit. para 3.8

<sup>73</sup> *Social Security Contributions and Benefits Act, 1992*, S. 5(1)(2)(3)

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Before 1980, the pension was updated by higher of the increase in prices or earnings. Because earnings tend to rise faster than prices, the National Insurance limits generally moved upwards in line with earnings. In 1980, the link between earnings and benefits was broken<sup>74</sup>, and benefits have been linked to prices only. A knock-on effect of this policy is that the earnings limits used to calculate National Insurance earnings limits have tended to fall in relation to earnings. These limits in turn are used in calculating "surplus" earnings for the purposes of SERPS entitlement.

With the limits falling in relation to earnings, the new formula in the bill, whereby surplus earnings are to be calculated with reference to the limits in force in the year in which they were earned, rather than the one prior to retirement, is likely to yield different rates of SERPS. For those earning below the upper earnings limit and above the lower one, the new formula for calculating surplus earnings will be less generous and will yield smaller SERPS entitlement than they would get under the current method of calculation. For those whose earnings are generally above the upper limit the situation can be reversed and the new formula could be more generous. In practice, most earners in SERPS are likely to be between the lower and upper limits and the overall effect of this change is to reduce spending on SERPS. The Government Actuary puts these savings at £1.3 billion by 2020, £2.5 billion by 2030 and £2.9 billion by 2040 (1994/5 prices)<sup>75</sup>. The change will affect everyone retiring with a SERPS entitlement after 6 April 2000 and will be applied to the whole SERPS calculation and not just that accruing after this date.

Discussion of this clause was limited in the Lords. For the Government, Lord Mackay of Ardbrecknish said the purpose of the clause was to correct an anomaly and restore the original policy intention that SERPS entitlements are based on average earnings between the lower and upper earnings limits. He outlined the effects of the change as follows<sup>76</sup>:

The present calculation revalues total earnings (up to the upper earnings limit) for each year in line with the increase in average earnings and then deducts the annual lower earnings limit for the last complete tax year from each year's revalued earnings to give a surplus for each year. Because the lower earnings limit grows in line with prices, SERPS entitlements have been growing in an unintended way. Annualisation will change the calculation so that the annual lower earnings limit is deducted before revaluation takes place. That simply means that when one looks back at a person's working life in each year the amount which is used for the revaluation calculation up to the date of retirement is the difference between the salary, if it is below the upper earnings limit, and the lower earnings limit. It will be on that portion above the lower earnings limit which will be revalued.

The current situation was not intended when the position was changed. The current situation is that the total and the lower earnings limit are revalued on a different basis. I shall not make any secret of the fact that this is not a small technical change. It is a technical change, but it is certainly not small. The change will result in a public expenditure saving of £400 million in 2010 rising to £2.3 billion by 2050. The maximum weekly reduction in

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<sup>74</sup> *Social Security Act 1980* S. 11

<sup>75</sup> Cm 2714

<sup>76</sup> *HL Deb* 20 Feb 1995 c1022

individual entitlements is estimated to be £2.70 in 2000, rising to £4.90 in 2020 at 1994-95 prices. This effect is a flat rate one and applies to those with a complete work history of earnings above the lower earnings limit since 1978. For those with broken work records the effects will be smaller. There will be no loss for people reaching pension age or who qualify for widow's benefits before 6th April 2000. This fulfils undertakings made during the passage of the 1986 Social Security Act that no changes would be made to SERPS this century.

Richard Disney and Paul Johnson of the Institute for Fiscal Studies have commented on the lack of protest that has been voiced about this overall reduction<sup>77</sup>. They see that as a reflection of the complexity and technical detail of the proposal as well as it being buried in a bill which also deals with equalisation of the pension age and wider regulatory issues.

In the Government Actuary's report on the Bill<sup>78</sup>, it was reckoned the long run effect of all the changes to SERPS is roughly to halve spending, from £19.3 billion in 2050 to £9.9 billion (all figures at 1994/5 prices). Appendix A reproduces the Government Actuary's detailed assessment of the financial effects of the Bill on the National Insurance Fund. In the long run about half the savings to SERPS arise through the changes to contracting-out expenditure, with equalisation of the pension age and change to the surplus earnings calculation accounting for around one quarter each of the total.

#### **4. Graduated retirement benefit**

Graduated retirement benefit (GRB) was the precursor of SERPS which was introduced in 1961, and wound up in 1975, although accrued rights were retained. The scheme yields very small pensions, partly because contributions made were not uprated in line with earnings (as they are with SERPS).

Paragraph 7 of Schedule 4 equalises GRBs for men and women, both for pensioners and widows/widowers.

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<sup>77</sup> Financial Times 3 Feb 1995 *The strange death of a pension scheme*

<sup>78</sup> Cm 2714

### II. War Widows' pensions

#### A. General background - help for widows

There are two potential sources of help for the survivors of armed forces personnel killed in service:

- **A War Widows' Pension** - A Department of Social Security (DSS) war widows' pension is available to a widow whose husband's death was the result of service.
- **The Armed Forces Pension Scheme** - A Ministry of Defence (MOD) administered occupational pension scheme for servicemen and their dependants. Survivors' benefits are available through this scheme.

Arguably, the recipients of DSS war widows' pensions (and indeed the war pension itself) are in a privileged position in relation to other social security claimants<sup>79</sup>. War widows' pensions (and war disablement benefits) are exempt from tax, whereas ordinary widows' pensions and retirement pensions are taxable. Under the "overlapping benefit" rules, it is not normally possible for a person to receive more than one income replacement benefit, so, for example, one cannot receive both invalidity benefit and a retirement pension. By contrast a disabled ex-serviceman can receive his war pension and a retirement pension. A war widow can receive a retirement pension based on her own contributions on top of a war widow's pension.

However, dissatisfaction is periodically expressed as a result of the way in which benefits paid to World War II veterans and widows compare with those paid to those from more recent conflicts. The discrepancies are the consequences of improvements which were made to the MOD Armed Forces Pension Scheme, particularly during the 1970s which were not retrospective. Those which are most relevant to widows are<sup>80</sup>:

- Improvements in 1973 to widows' benefits;
- The introduction of pensions for widows of post-retirement marriages in 1978.

Before the 1973 improvements to the Armed Forces Pension Scheme, cited above, war widows could only receive a DSS pension or a Forces pension based on her husband's service, whichever was greater. After 31 March 1973, war widows were allowed to keep both pensions. There was criticism at the time that a differential had been created between the two groups of widows.

Governments of both parties have generally argued that it is a long-standing principle of occupational pension schemes that such improvements should not be made retrospective.

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<sup>79</sup> For a full discussion of this issue see *The Law of Social Security*, Ogus and Barendt, 1995, pp 349-53

<sup>80</sup> See Archie Hamilton, then Armed Forces Minister in an Adjournment Debate HC 23 5 91 c1125

However, the resulting differences of treatment have led to groups representing service personnel to lobby for the benefits to be extended to people who served before the changes.

Following a successful campaign on behalf of war widows, special MOD payments to "pre-1973" widows were introduced by the then Defence Secretary, Tom King, in December 1989. A tax-free payment of £40 per week was introduced in April for all such widows. This now stands at £49.77 per week. This is disregarded completely in benefit calculations. This does not necessarily represent complete parity, but it is certainly a retrospective improvement.

There have been other improvements to DSS benefits for war widows. In 1979 the war widows' pension was made tax-free. In 1984 a new tier of age allowance was introduced to provide additional money for war widows aged 80 or over. There are now age allowances for all widows aged 65 or over. In 1987, extra help for funeral costs was made available to war widows.

More recently, the Government has announced a concession for British widows of New Zealand servicemen which will bring their pensions into line with UK pension rates. This small group previously received a lower pension because their husbands served with the independent New Zealand Forces during the World War II. Also special payments made to certain widows of servicemen killed in Northern Ireland have been raised to bring them into line with the special payment made to pre-1973 widows<sup>81</sup>.

## **B. The current campaign**

The Officers' Pension Society and the War Widows' Association are currently campaigning for further improvements to the benefits available to war widows. There are three main claims:

- **To give war widows a pension for life**, ie. not to lose entitlement to a widow's pension on remarriage (as happens now);
- **To award widows a pension half the value of that of their late husband's**. Half-rate pensions were introduced for widows of those retiring after April 1973 if their husbands bought into the improved scheme. However, one-third pensions remained for widows of those retired before this date. The current campaign is for all widows to be given half pensions regardless of the date of retirement of their husbands (and irrespective of whether they contributed to these enhanced provisions);
- **Provision of widows' pensions for those marrying after retirement** (but before 65) from the services. It has been possible since April 1978 for women who married their husbands after they had retired from the Armed Forces to receive a widow's pension. This improvement resulted from Section 36 of the Social Security Pensions Act 1975, which

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<sup>81</sup> See HC Deb 23 June 1994 c 255W

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required all schemes which are contracted out of the State Earnings Related Pension Scheme to provide widows' pensions regardless of the date of the marriage. As the Armed Forces Pension Scheme is contracted out its rules were amended, with effect from 6 April 1978.

The campaign has been widely supported in the Commons, evidenced by the number who have signed the Early Day Motion - EDM 86 - which had attracted 245 signatories at 19 April 1995.

### EDM 186

That this House calls attention, in this 50th anniversary year of victory in the Second World War, to the proposals by the Officers' Pensions Society and the War Widows' Association of Great Britain, wholly supported by the Confederation of British Service and Ex-Service Organisations, to honour the dead of two world wars and the campaigns since 1945, by paying Britain's war widows a pension for life and the widows of servicemen a pension of at least half of their late husbands; and urges Her Majesty's Government to make a positive response to proposals which command such warm and widespread support throughout Britain.

### C. The Bill's proposals

117. A widow of a member of Her Majesty's forces whose death in service or retirement was adjudged to be attributable to service, who presently loses or has lost her War Widows pension on remarriage, shall on second bereavement or failure of the second marriage have her DSS War Widows Pension (and in the case of a widow of a deceased member of Her Majesty's forces who retired or died in service before 31st March 1973 also her DSS ex gratia supplement) restored automatically.").

**Clause 117** of the Bill was inserted as a result of a Government defeat in the Lords<sup>82</sup>.

It partly addresses the first of the claims by the Officers' Pension Society and War Widows' Association and proposes that the DSS War Widows' Pension should be reinstated to a widow who had previously lost the pension on remarriage if that marriage fails.

At present, war widows who re-marry lose entitlement to a widow's pension. This is a common element of many public (but not private) sector pension schemes<sup>83</sup> and it is argued that such pension rights should be restored if the second marriage ends in bereavement or divorce or fails for some other reason. Younger widows (those with a service pension from the MOD) can apply for pension restoration in these circumstances, although this is subject to a means test.

The Government response has been that the loss of pension on remarriage is analogous to the national insurance widow's pension. The MOD position (for those with a service pension) reflects that of other public sector pension schemes<sup>84</sup> where discretion is normally exercised if the widow is financially worse off at second widowhood than when she was first widowed.

The "ex gratia supplement" in the clause refers to the special payments, currently of £49.77 pw, which were awarded to pre-73 widows in 1989 (described on page 29). In responding to the debate on the clause in the Lords, Lord Mackay of Ardbrecknish (Minister of State for Social Security) pointed out the tax-free supplement was not *ex gratia*, but a payment introduced via legal provision<sup>85</sup>.

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<sup>82</sup> HL Deb 14 March 1995 c767

<sup>83</sup> GAD *Occupational Pension Schemes 1991, Ninth Survey*

<sup>84</sup> HC Deb 21 Feb 1995 c258

<sup>85</sup> HL Deb 14 March 1995 c782

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### D. Defeated amendments

#### 1. Post-retirement marriages

Two further amendments<sup>86</sup> were introduced in the Lords which would have addressed points in the current campaign by the Officers' Pension Society and the War Widows' Association.

**Amendment 186** called for all service widows (ie. those whose husbands were members of the Armed Forces Pension Scheme) to receive a full pension even if they married their husbands after they had retired from the forces (providing it was before he reached 65 and the marriage had lasted at least 3 years.) Currently, only those with service after 6 April 1978 qualify for this provision. The amendment would have eliminated this cut-off point. **This amendment was defeated.**

#### **Amendment 186 - Service Widows pensions: post-retirement marriage**

No widow of a member of Her Majesty's forces shall be disqualified from receiving a full pension in relation to the deceased's membership of Her Majesty's forces by virtue of the fact that her marriage occurred after the deceased member had retired from Her Majesty's forces provided that the marriage took place before his 65th birthday - the end of his recall liability - and has lasted for at least three years.

HL Deb 14 March c786

#### 2. Pensions for life

The intention of **Amendment 191B** was to give widows the right to continue to receive their DSS War Widows Pension and Armed Forces Service pension regardless of any change in status. It was to stop widows losing their pensions if they remarry or cohabit. **This amendment was defeated.**

#### **Amendment 191B - War Widows Pensions**

The widow of a deceased member of Her Majesty's forces whose death was adjudged to be attributable to service shall continue to be entitled to a war widows pension regardless of any subsequent changes of status.

HL Deb 21 Feb 1995 c1067

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<sup>86</sup> Numbers 186 and 191B

Appendix A - Government Actuary's Estimates - Cm 2714

**Table 1 Estimated cost of National Insurance benefits**

(£ billion at 1994-95 prices)

	2000-01	2010-11	2020-21	2030-31	2040-41	2050-51
<b>Existing scheme</b>						
Retirement pensions:						
Basic Pension	29.8	33.7	39.8	46.9	48.2	46.6
Earnings-related pension	4.2	9.2	14.5	18.7	19.5	19.3
Widows' benefits:						
Flat-rate	0.7	0.6	0.6	0.5	0.5	0.5
Earnings-related	0.2	0.1	0.1	0.1	0.1	0.1
Incapacity benefits:						
Flat-rate	5.1	6.2	6.6	6.3	5.9	6.0
Earnings-related	0.6	0.1	—	—	—	—
Other benefits	1.7	1.7	1.8	1.8	1.8	1.8
<b>Total</b>	<b>42.2</b>	<b>51.7</b>	<b>63.4</b>	<b>74.2</b>	<b>76.0</b>	<b>74.2</b>
<b>After proposed changes</b>						
Retirement pensions:						
Basic Pension	29.8	33.6	35.2	41.9	44.5	42.3
Earnings-related pension	4.2	8.4	10.9	12.0	10.2	9.9
Widows' benefits:						
Flat-rate	0.7	0.6	1.2	1.1	0.9	1.0
Earnings-related	0.2	0.1	0.1	0.1	0.1	0.1
Incapacity benefits:						
Flat-rate	5.1	6.2	7.2	6.9	6.4	6.5
Earnings-related	0.6	0.1	—	—	—	—
Other benefits	1.7	1.7	1.8	1.8	1.8	1.8
<b>Total</b>	<b>42.2</b>	<b>50.8</b>	<b>56.4</b>	<b>63.8</b>	<b>63.9</b>	<b>61.7</b>

Note: individual components may not sum to totals due to rounding.

30. Table 1 indicates that, on the basis of today's prices, substantial increases may be expected in future in the cost of benefits payable from the National Insurance Fund. This is as would be expected for SERPS, where the numbers entitled to pensions based on earnings since 1978 are still building up and earnings are assumed to grow steadily at 1½ per cent a year more than prices. The increase in the cost of the basic retirement pension reflects the changing demographic structure of the population, with an increasing number of people reaching retirement age, particularly in the period 2010 to 2030, as the cohorts born in the 1950s and early 1960s, when the birth rate was rising rapidly, attain pension age. The change in female pension age reduces the number of retirement pensioners by about 2 million in 2030, as can be seen in Appendix E. However the estimated number of pensioners in that year is still about 40% greater than at present.

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**Table 2 Estimated financial effect on the National Insurance Fund of the proposed changes**

	(£ billion at 1994–95 prices)					
	2000–01	2010–11	2020–21	2030–31	2040–41	2050–51
<b>BENEFIT CHANGES</b>						
Changes to State Pension Age						
Basic Retirement Pension	—	–0.2	–4.7	–5.0	–3.9	–4.3
SERPS	—	–0.03	–1.7	–1.9	–1.8	–2.6
Widow's Pension	—	+0.02	+0.6	+0.6	+0.5	+0.5
Incapacity benefit	—	+0.03	+0.6	+0.6	+0.5	+0.6
Other NI benefits	—	0.0	+0.1	+0.1	+0.1	+0.1
Changes to graduated retirement benefit, increments and dependency conditions		0.0	+0.1	+0.1	+0.1	+0.1
Inclusion of Family Credit and Disability Working Allowance in earnings factors	0.0	0.0	+0.01	+0.06	+0.1	+0.1
Changes to SERPS calculation	0.0	–0.6	–1.3	–2.5	–2.9	–2.7
Changes to contracting-out SERPS expenditure	0.0	–0.1	–0.7	–2.4	–4.7	–4.2
<b>NI CONTRIBUTION CHANGES</b>						
SPA change	—	0.0	–0.1	–0.1	–0.1	–0.1
Changes to contracting out						
—assuming 4.6% rebate	+0.4	+0.6	–0.1	–0.8	–1.1	–1.1
—assuming 4.95% rebate	+0.9	+1.1	+0.4	–0.3	–0.6	–0.6

Notes: 1. The above figures break down the total change in benefit expenditure shown in Table 1 into the effect of each separate proposal in the Bill. The sum of these changes may not agree with the total change in Table 1 due to rounding.

2. Positive figures denote higher expenditure or lower contribution income. Negative figures denote lower expenditure or higher income. The estimates therefore show the effect on the financial position of the National Insurance Fund.

3. All figures for future years should be read in conjunction with paragraphs 32 to 33 regarding uncertainty.

Papers on related subjects have been:

95/46 The Pensions Bill 1994/5: Pension Fund Regulation

95/48 The Pensions Bill 1994/5: Occupational Pensions

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