MT

S
808

Confidential Filing

CPRS Report on Pensions.

CPRS Papers on "Pensions and Individual Choice" and "Pensions Issues and Policy".

ECONOMIC POLICY

March 1983.

Referred to	Date	Referred to	Date	Referred to	Date	Referred to	Date
~~5-7-83~~ 29.7.83							

PREM 19/1004

DEPARTMENT OF HEALTH & SOCIAL SECURITY

Alexander Fleming House, Elephant & Castle, London SE1 6BY

Telephone 01-407 5522

From the Secretary of State for Social Services

PERSONAL

Robin Butler Esq
Principal Private Secretary
10 Downing Street

29 July 1983

Pl. file

Dear Robin

Thank you for your letter of 27 July and for sending me copy number 17 of the further CPRS paper entitled "Pensions and individual choice". At present we see no need for anybody other than the Secretary of State, myself and Michael Partridge to see the papers. I will let you know if we wish to extend the circle any further.

Yours
Steve

S A Godber
Private Secretary

file

10 DOWNING STREET

From the Principal Private Secretary

27 July 1983

PERSONAL

At the Prime Minister's request, I gave your Secretary of State copy No. 16 of a CPRS paper entitled "Pensions: Issues and Policy". The Prime Minister asked your Secretary of State to ensure that only he and one or two named officials had access to this paper, of which no copies should be made. Could you please drop me a line and let me know the names of those who will be given access to this paper.

BF

E. E. R. BUTLER

Steve Godber, Esq.,
Department of Health and Social Security.

10 DOWNING STREET

Michael

—

Draft CPRS paper, obtained from them today.

Peter
5/7

✓CC NO

This is a disaster and MUST NOT go any further. It is arrogant, insensitive and impossible.

Please ask Sir Robert Armstrong & Mr. Sparrow to see me on Monday

Prime Minister

These lengthy papers are summarised at Flag A (pp 2-4)

MCS 22/4

CONFIDENTIAL

Qa 06343

To: PRIME MINISTER

From: JOHN SPARROW

22 April 1983

Pensions

1. You asked to see the results of our work on pensions before deciding how they should be handled and circulated. The remit for our work was set out in my minute to Robin Butler dated 6 October last year.

2. As our work progressed we were increasingly impressed by the complexity of the subject and the need to bring together a number of studies by officials on specific aspects of pensions (e.g. the burden of pensions, disclosure by occupational schemes, response to Social Services Committee recommendations on early retirement, etc.). We therefore decided that our most useful contribution would be a general paper surveying the full range of issues, suggesting objectives for Ministers and outlining the practical implications of these for pensions policy. This paper, with the title "Pension Issues and Policy", provides a framework within which the various individual items of work currently in progress can be assessed. It also identifies three other possible areas for study which are not being covered by current work.

3. "Pension Issues and Policy" does not pull any punches and you will certainly find it politically sensitive. The issues are real and will not go away. They are issues which Ministers collectively need to consider - especially if they are to make a sensible response to the various detailed reports coming forward to them in the coming weeks.

4. In response to that part of the remit covering scope for greater individual choice we have written a separate paper "Pensions and Individual Choice". We have recently learned that a Tory Party

Study Team will shortly be making some proposals in this area. The problem is complex and I suggest that Ministers should consider the results of our own work before any public commitment is made about the results of the Party work.

5. You should know that we have had some informal contacts with a few individually nominated officials in the DHSS, Treasury, Government Actuary's Department and Inland Revenue to discuss our work.

6. I thought you would want me to send a copy of this minute and attachments to Sir Robert Armstrong.

JS.

Atts

CONFIDENTIAL

Spare copy in Folder

Copy No 16

PENSIONS AND INDIVIDUAL CHOICE

A Paper by the CPRS

April 1983

CONFIDENTIAL

CONTENTS

CONTENTS (continued)

ANNEX - SOME OF THE PROBLEMS INVOLVED IN THE PORTABLE OCCUPATIONAL PENSION

PENSIONS AND INDIVIDUAL CHOICE

SUMMARY

1. The present occupational pensions system (paragraphs 3-9):

- tends to discriminate against the 'early leaver' i.e. the person who changes jobs. This is less and less appropriate if the economy is to develop flexibly and vigorously.

- tends to result in individuals having little awareness of or interest in the investments which actually fund their pensions.

- usually gives the employee no choice in how he provides for his retirement.

2. Greater equity, labour market flexibility and visibility could be achieved by developments within the existing system - by better treatment of early leavers, greater use of 'money purchase' and S.226 schemes etc. But if individual choice and responsibility are to be widened and if the individual's perceived stake in profitable enterprise is to be increased, a new route is needed (paragraphs 10-20). We propose the Portable Occupational Pension (POP).

3. POP is an individual pension scheme (paragraphs 21-24):

- to which both employer and employee contribute.

- which aims (but does not guarantee) to provide a specific replacement income throughout retirement.

- of which the benefits are based on contributions made and on performance of the accumulated fund.

4. The POP presents a number of possible problems (paragraphs 25-28 and Annex). Because of these problems, and the difficulties always inherent in making major changes in the pensions field, we suggest an evolutionary approach.

5. We do not advocate the 'unitisation' of all existing pension funds into POPs because this would effectively force everybody to become an "early leaver", and so those who do in fact stay in their present employment until retirement would be deprived of their current expectations of benefit. We do not advocate giving employees the right to opt out of occupational schemes and make their own individual provision - at least, not yet. We prefer a voluntary approach, so that demand for POPs can evolve naturally in those occupations most suited to it. Only if subsequently there was a demand for POPs which was being thwarted would we advocate legislation (paragraphs 29-36).

6. We list a number of detailed recommendations designed to help the POP, which is already feasible, to flourish more widely within the existing pensions and fiscal framework (paragraph 35).

7. We believe that, even with extended availability of POPs, the larger pooled pension schemes (public and private) would still be offering a deal which the majority of their members will find preferable to POPs. Thus pooled occupational pension schemes would still remain the core of good private pension provision. The competition from POP should improve the visibility of all pension provision. The increase in personal choice, plus the increased visibility, should awaken wider interest in the success and efficiency of the capitalist system. We do not, however, expect there to be a major reduction in the concentration of capital; most individuals will want to invest through intermediary institutions (paragraphs 37-42).

PENSIONS AND INDIVIDUAL CHOICE

INTRODUCTION

In an accompanying paper 'Pensions Issues and Policy' the CPRS has proposed objectives for pensions policy and suggested how those objectives, if accepted, might be reflected in policy changes. We suggested, inter alia, that reforms were needed in the occupational pensions sector.

2. In this paper we -

(i) discuss some of the problems in occupational pension schemes at present (paras 3-9);

(ii) suggest five aims for policy in this field (para 10);

(iii) list a number of possible developments which might help to meet some of the policy aims (paras 11-20);

(iv) describe the Portable Occupational Pension (POP) as a method of achieving the policy aims, and explain its advantages and drawbacks (paras 21-28);

(v) outline a strategy for encouraging the development of the POP, with recommendations for action (paras 29-36); and

(vi) set the POP in the context of the current partnership between state and occupational pensions (paras 37-42).

SOME PROBLEMS IN OCCUPATIONAL PENSION SCHEMES

The early leaver and labour mobility

3. Employers have shaped pension schemes as instruments of management. Pensions are used not only to ease the process of retirement but also as an attractive employee benefit to aid recruitment and to encourage employees to stay until retirement. The Social Security Act 1973 compels occupational schemes to preserve until retirement the pensions of those who leave with more than five years service and are over 26. Unless the employer chooses to do something towards maintaining the value of the pension, the early leaver will have no protection against inflation other than that which he receives from the state Earnings Related Pensions Scheme (SERPS).

4. Thus, for the 6m private sector employees in occupational schemes, the higher inflation of recent years has established a major disparity between the pensions of long-service employees and of those who move around - early leavers. (People who move around within the public sector avoid this disparity because they benefit from a transfer club). Private sector employees who leave before retirement are often regarded as exceptional. Yet the average employee changes jobs on average three or four times in his lifetime. A survey of 39,000 retirees in the 1970s from schemes managed by a leading insurance company showed -

Years service with last employer	%
Over 30 years	25
21-30	21
11-20	29
6-10	18
0-5	7

5. There is some evidence that accumulated pension rights are associated with lower mobility. This is what one would expect, since the private sector employee of 40 or over who wants to change job or become self-employed or

start his own business, and who has occupational pension rights significantly better than those given by the state scheme, will normally find that pensions considerations are an obstacle to a move in any direction. Any move will involve a substantial penalty, the devaluation of his pension rights accrued to date, even given modest rates of inflation.

6. The CPRS considers that over the next decade the UK economy needs to become more flexible in organisation and employment patterns. The UK will need to adapt to a fast pace of technological change as well as to changes in the international division of labour and in markets. The larger organisations, which constitute the primary sector of the economy, will need to employ fewer people in relation to output and to transfer parts of their activities to the secondary sector; and if the primary sector is to be vigorous and adaptable, there will need to be greater labour mobility within it and between it and the rest of the economy. Moreover, the strength of the economy, and the number of people employed in it, will depend increasingly on the imagination, energy and courage of those who make new starts within the secondary sector, whether as employees or employers. Today's pension system needs to take this into account.

The pensions promise

7. To be contracted out of the SERPS occupational pensions schemes must offer the 'requisite benefits' as defined by the Social Security Pensions Act 1975: pensions, accruing at the rate of at least 80ths, must be related either to final salary (as in the great majority of cases) or to revalued average annual salary. These types of scheme are in contrast to so-called 'money purchase' schemes under which the value of the benefits received will be determined solely by the amount of contributions paid and the value of the fund. Such schemes can be severely attacked by inflation and the final salary scheme, with its promise of benefits related to income on retirement, seems much more attractive. In practice of course, as with money purchase, total benefits paid out under a final salary scheme must relate to the value of the underlying fund - unless (as has often occurred in recent years) the employer chooses to make topping-up contributions to the fund. Even so, the

benefits offered by private sector final salary schemes are often not what they seem. Inflation proofing of pensions in payment is often poor and sometimes non-existent; in recent times many people have retired with a reasonable pension but then seen it dwindle rapidly in value. It would probably have been better if such people had had lower initial benefits which were then better protected against inflation. It would certainly have been better if they had understood all along the nature of the pension promises made to them, so that they could, if they chose, have made additional provision for their old age.

The individual and pension funds

8. Occupational pension schemes are now supported by funds worth about £120bn. About half those funds are invested in UK equities. The funds are effectively controlled by employers, or jointly by employers and representative bodies (including trade unions), and the individual pension scheme member has little or no knowledge of them. For the individual the pension promise is made by the employer, and the funds are simply a mechanism by which this is implemented. In this way the underlying investments become a closed circle, with companies (and public corporations) through their pension funds investing in other companies. The individual employee does not feel that he has an interest in the pension fund and the performance of its investments. There is no mechanism by which he is able to see that his standard of living in retirement will depend on the success of profit-making enterprise. And the pension funds remain vulnerable to political direction.

Freedom of choice

9. In about nine cases out of ten, members of occupational schemes have been compelled by their employer to join. This has been an understandable response by employers to the possibility that employees would opt out of schemes if they were voluntary and would become, in retirement, cases of hardship with claims on the employer which he would find hard to resist. Compulsory membership also allows insured schemes to obtain better rates for death and ill-health benefits. However the present situation deprives the average employee of responsibility and of choice in relation to what may well be the largest - or certainly second largest - investment in his life - namely, saving for retirement.

POLICY AIMS

10. Having regard to the problems mentioned in paragraph 3-9 above, we consider that it would be desirable to develop, within the occupational pensions sector, the means of -

(i) improving equity between members of pension schemes;

(ii) increasing the flexibility of the labour market;

(iii) increasing the visibility of pension arrangements and employees' interest in them;

(iv) widening individual choice and responsibility; and

(v) increasing the individual's perceived stake in profitable enterprise.

In the following paragraphs (11-18) we describe some possible developments in pension provision which are already on the agenda and which may go some way to meet the aims set out above.

POSSIBLE DEVELOPMENTS

Better Transferability in the Private Sector

11. The concerns about equity and labour mobility (para 10(i) and (ii) above) would be eased if the pensions industry moved voluntarily to improve the position of early leavers so that preserved benefits were increased in line with national average earnings. This is unlikely. The most that can be hoped for is that many schemes will implement at least the minimum recommendations of the Occupational Pension Board (OPB)'s report on early leavers, i.e. in respect of future service schemes should revalue preserved pensions by 5% a year. By 1984 some schemes will have moved voluntarily in this direction. But because the early leaver is not generally favoured by employers, legislation will be required to achieve this route to transferability. We recommend it, at para 35.I. below.

12. In principle all private sector schemes might become transferable on the lines of the public sector transfer club, with pensions reflecting final salary and based on a complete career. A small number of schemes (eg Motor Agents Scheme) are in this form. However it is most unlikely that many employers will voluntarily move in this direction since it carries certain increased costs and uncertain advantages. Full implementation would have to be by legislation, which we do not recommend.

13. Leading individuals in the pensions industry have put forward proposals for a Central Fund for Early Leavers, which are now being considered in DHSS and DoT. In principle this fund could do nothing for early leavers that insurance companies could not do if they offered investment of transfer values in a balanced portfolio, rather than translation into deferred annuities. And the fund does not itself improve the transfer values initially receivable by the early leaver, which are based on his accrued rights to a preserved pension. It also has other major disadvantages, in particular that of being a major investment institution attached neither to an employer (like pension funds) nor to other recognized bodies (such as insurance companies).

Movement to money purchase, or combined money purchase/final salary schemes

14. Another approach to the evolution of the pensions system would be to encourage the greater use of money purchase schemes by employers. These schemes, referred to briefly at para 7 above, have rather fallen into discredit because of their inadequate response to inflation. We believe, however, that it is no longer sensible to regard money purchase schemes as second best, provided they have satisfactory contribution rates. Money purchase schemes can be devised to achieve some of the aims set out in para 10 above. Schemes which provide annual individual benefit statements bring employees closer to their savings, and knowledge of these savings may be a source of satisfaction and of interest. Furthermore money purchase schemes are equitable as between employees. They are also particularly suitable for industry-wide schemes where no one employer can take on the whole final salary commitment. Moreover, it is perfectly possible for money purchase schemes to be funded by a substantial margin over that required to meet the Guaranteed Minimum Pension (GMP) requirement*. We consider that such schemes should be allowed to contract out of SERPS; this will require legislation to alter the 'requisite benefits' provisions of the 1975 Act (see para 7 above).

15. But many employers and employees may wish to retain the benefits of a final salary promise. One recently announced scheme, the London and Manchester "Combine" scheme, provides money purchase benefits for those who leave, and final salary benefits for those who stay. We endorse this approach, which is compatible with contracting-out under current rules, but note that to achieve its twin objectives it requires higher contribution rates (at a given level of target benefit) than conventional money purchase or final salary schemes.

---

* Occupational pension schemes which are contracted out of SERPS are obliged to provide a Guaranteed Minimum Pension.

Additional Voluntary Contributions

16. Members of occupational pension schemes are entitled to supplement their provision, up to Inland Revenue limits, by having Additional Voluntary Contributions (AVCs) paid to an intermediary and aggregated with their employer's scheme. There is a germ here of individual responsibility which should be fostered. For this reason we consider it desirable that employers should arrange their AVC facility with a number of intermediaries and should encourage individuals who wish to make AVCs to choose the intermediary themselves rather than have it imposed on them.

17. Greater individual AVC provision would be only a supplement to conventional occupational pension provision, rather than an alternative to it. It is principally suitable for the final years of employment when the adequacy or inadequacy of employer provision can be assessed. It mitigates, rather than eliminates, the inequities of final salary provision for the early leaver.

"Section 226" Schemes

18. Since 1956 both the self-employed and employees outside occupational schemes have been able to make individual pension provision on a tax-exempt basis through insurance companies under what are now known as S.226 contracts. Individual provision through S.226 schemes, principally by the self-employed, is growing fast; the number of policies in existence doubled between 1977 and 1981. The employer is not allowed to contribute to these contracts although he may be persuaded to increase an individual's salary to achieve the same end. This is a major disadvantage. Because the bulk of private pension provision has been initiated by employers a route which excludes employer commitment and responsibility is unlikely to offer serious competition to conventional occupational pensions provision.

Disclosure

19. Ministers have already accepted in principle that there should be legislation to enforce adequate disclosure by pension funds of information about their assets and funding status. An Official Working Group will be reporting to Ministers shortly about implementation of the Occupational Pensions Board's recommendations on this subject. Improving disclosure by funds should help significantly to further the aim - paragraph 10 (iii) - of increasing visibility of pension arrangements and employees' interest in them, and of developing a constituency which would resist political direction.

PORTABLE OCCUPATIONAL PENSION

What is a POP?

20. In paragraphs 11-19 we have mentioned some measures - principally on early leavers, on money purchase schemes, and on disclosure - which should improve the occupational pensions system and further some of the aims set out in paragraph 10. But even if the Government were to encourage and, where necessary, implement these measures, they would do little to meet the last two aims mentioned in paragraph 10 - those of widening individual choice and responsibility, and increasing people's stake in profitable enterprise. We have therefore explored the merits of another route which might meet all the aims we proposed. This route is the Portable Occupational Pension (POP).

21. The POP is an individualised pension scheme. Each participant has his own individual pension plan which is provided by a financial institution such as an insurance company. When the employee leaves his job, he can take his individual pension with him. The POP would have the following additional features -

(i) Both employer and employee would make significant contributions, thus retaining the tradition of employer commitment to occupational pension provision.

(ii) Schemes would be money purchase or, as we prefer to call them, 'defined contribution plans' in the sense that the value of the accumulated fund at retirement would be based on the record of contributions, as increased by investment. This fund would be crystallised into one or more annuities at or after retirement to provide a pension. The level of contributions could be variable and in particular would be varied as retirement approached with the aim of providing at retirement a pension which was not guaranteed but which came as near as possible to a target level of income replacement.

(iii) Schemes would normally be marketed through employers to minimise costs and achieve employer acceptance. The individual would initially be offered the choice between, say, three individual plans offered by financial institutions which are now permitted to solicit investments from the public. However, individuals who wished to save with another body, and new entrants bringing a POP with them, should be allowed to make that choice, subject to an extra charge to reflect administrative costs.

(iv) Individuals could contribute to one POP at any one time. They would be free to start a new POP with a new intermediary, but there would be no presumption that the funds previously accumulated would be transferable to a new intermediary.

(v) Schemes would need to be approved by the Superannuation Funds Office of the Inland Revenue, who would need to be satisfied that the intermediary responsible for each POP was a responsible body, able to police Inland Revenue limits on benefits in the way that the employer normally does. In practice the Inland Revenue would exercise control principally through contribution rates but, because the POP is an occupational scheme, it would be possible to increase contribution rates near to retirement, provided that benefits, when aggregated with other retained benefits, did not exceed two-thirds of the employee's final remuneration.

(vi) It would also be desirable, but not essential, that the DHSS and the OPB should seek to facilitate arrangements to allow well funded individual POP schemes to contract out of SERPS. This should be done by allowing approved intermediaries to satisfy the OPB that the rate of contributions was generous enough to be well able to satisfy reasonable requirements as to the GMP. In such cases the employer's rebate on the National Insurance Contribution should be payable into the fund supporting the POP.

22. It is worth noting that it is already possible for individuals to take out individual occupational pension plans with their employer and, if certain restrictive conditions are met, for such plans to be contracted out of SERPS. Few of such plans are designed to be portable and we know of only one such plan outside the insurance industry, the Richards Longstaff Independent Pension Plan, launched in 1979 for directors and senior executives. The Superannuation Funds Office approves a central trust deed for such plans, so that when the individual changes job, the new employer simply has to sign a deed of adherence to the plan.

23. The POP, if it became widespread, would do much to further the aims set out in paragraph 10 above -

(i) it would improve equity between pension scheme members by eliminating some of the most serious cross-subsidies inherent in the present system, e.g. between early leavers and stayers;

(ii) it would increase labour market flexibility by reducing the penalties which the present system imposes on those who move jobs or who move from employment to self-employment;

(iii) it would increase visibility because the very availability of POPs would stimulate interest in pensions and require the pension funds to explain and justify some of their existing practices;

(iv) it would widen individual choice and responsibility since employees could choose from a range of pension schemes; and

(v) it would increase the individual's perceived stake in profitable enterprise since those opting for POPs would appreciate that their ultimate pension would depend on the performance of the investments underlying the POP.

24. There are, however, problems too. These are set out in detail in the Annex to this paper and are summarised in paragraphs 25-28 below.

Problems over POPs

25. First, if POPs became widespread, there could be a reduction in the overall level of pension provision, since employers would have a lesser incentive to set up or continue to run their own company pension schemes. In some cases their employees could end up contributing to SERPS. It is debatable how far this would be a problem. A reduction in total pension provision might actually be desirable; and a modest degree of transfer from funded company schemes to the State's pay-as-you-go scheme might be an acceptable price to pay.

26. Second, unlike occupational pension schemes, the POP could not guarantee a level of benefit which is related to final salary. In practice, a final salary target should be achievable in normal circumstances, if that is what is wanted, by appropriate adjustment of contributions. Problems would however occur (as indeed they occur for ordinary pension funds) if inflation increased rapidly or if the future pensioner obtained large real increases in pay shortly before retirement. There is however no reason at all why POP benefits in retirement should be protected against inflation any less well than occupational pensions are.

27. Third, in the transitional period before POPs became widely established, problems would be caused by the large differences in 'real' contribution rates in respect of employees of different ages or ages of entry. Younger employees who would naturally be most interested in POPs would face the prospect that, as they grew older, their employer might well be unwilling to pay the increasing rates of contribution necessary to fund the pension. Many employees might therefore be deterred from the POP route. On the other hand, withdrawals from occupational schemes into POPs on any scale might pose problems for the schemes. In our view, however, only the smaller, insured schemes would be at risk if POP spread widely.

28. Fourth, individual pension provision is necessarily more costly to administer than pooled pension schemes. At least initially it would be possible for employers to limit these extra costs; but if POPs became

widespread, so that employers had to deal with a large number of intermediaries (insurance companies etc), and with individualised contribution rates, the extra costs could be substantial. Employers would probably insist that these were largely met by a reduction in the individual's benefit.

STRATEGY FOR THE POP

29. There are therefore important problems in POP and particularly in making the transition from the present position to one where POP was widespread. Furthermore Government would face the political difficulties of certain opposition from the pensions industry if it outlawed the compulsory occupational pension scheme, and concern among a large number of older employees and pensioners about any weakening of occupational pension schemes. Nonetheless we believe that the Portable Occupational Pension fulfils the objectives set out in paragraph 17 of the accompanying paper 'Pensions Issues and Policies' more aptly than the existing system of occupational provision and that it is desirable that it should be widely available, if this can be achieved without undue transitional difficulty. We now therefore discuss how the Government might encourage the development of POPs.

30. We are <u>not</u> advocating a radical transformation of the occupational pension system into one principally or entirely based on the POP. This would not reflect the current wishes of the bulk of potential pensioners, let alone employers, and it would be unreasonable to impose it on them. Our aim is to make the POP a realistic alternative which is available for those who wish to take this route - initially comparatively few, probably the more mobile and financially sophisticated who are best able to take decisions about long-term financial commitments. But the occupations for which it is particularly appropriate may be the growing ones and ultimately this route might become more common and spread from the minority to the majority as home ownership has done.

31. We have identified three main ways that could be used to encourage the spread of the POP -

Option I introduce legislation to 'unitise' the existing pooled pension funds, such that each employee could choose to transfer the value of his accumulated pension rights to a POP; or

Option II introduce legislation to give all employees the choice to have future pension contributions made to a POP; or

Option III create conditions in which employees in certain kinds of employment might be more likely freely to negotiate a POP alternative with their employer.

32. We see serious difficulties in option I. Under the terms of pension schemes employees have the right to final salary benefits if they stay to retirement and to lesser benefits if they leave. In practice, because of mobility, few members of a scheme will stay in the same employment through to retirement - indeed contribution rates for schemes are calculated on this assumption. In principle, though, each member has the right to, or expectation of, a final salary benefit. Hence the aggregate value of members' rights and expectations substantially exceeds the value of the fund. There is no one way to measure each employee's share in the fund. If his existing expectations were to be fully respected, an estimate would have to be made of the chances of his staying to retirement, of projected rates of inflation and of salary progression. This creates two principal problems for unitisation:

(i) If the value of any employee's share at the moment of unitisation did not reflect the value implied by his right to stay until retirement with a typical career progression, unitisation would fail to respect the rights and expectations that any individual scheme member reasonably has.

(ii) If the value of any employee's share at the moment of unitisation were based simply on contribution record, then older employees with fewer years of service to retirement would be penalised more than the younger employees with a greater probability of leaving.

33. It can be argued that these problems of unitisation are similar to those which would arise from legislating to implement the OPB report on early leavers. Although it might be preferable to offset the costs of implementing the report by reductions in final salary promises this would be resisted by scheme members. In most cases therefore the cost would have to be borne by the fund itself or by increased contributions (in practice these would tend to come from the employer). But unitisation has the additional disadvantages:-

(i) There is no possibility (as there is under the OPB recommendations) that the costs of shielding employee's expectations might be borne by the fund or by the employer.

(ii) It puts all employees into the position of early leavers at the point of unitisation, and hence those who do in fact stay in their present employment until retirement are deprived of their current expectations of benefit (based on a higher final salary, due to career progression, multiplied by an unbroken record of service).

34. Nor can we recommend option II at the present time. This is because there is currently no constituency for the POP and there are substantial vested interests among potential pensioners, employers and the pensions industry which would be concerned about its effect on existing rights. To make it effective employers would have to be required to estimate for each employee the contribution made on his behalf, and offer him the choice as to whether to invest this within the pooled scheme or individually. If a disproportionate number of potential leavers opted out (as would be likely) then the remaining contributions would be insufficient to pay for the final salary promises of the stayers, unless employers topped up the fund. The problems are similar, albeit on a smaller scale, to those outlined in paragraph 33 above. And we are doubtful whether the alternative intermediaries, notably the insurance industry, are currently equipped to sell individual pensions business on a realistic basis, except to the financially sophisticated or in co-operation with the employer. However we do not rule out the possibility of legislation in the long term.

35. Our approach would therefore be that of option III, even though this would take much longer to develop. We set out below a number of steps which the Government could take to encourage the development of the POP:

A. We recommend that the feasibility of the POP should be communicated more widely, both by Ministers when they speak on pensions issues and by the Inland Revenue in its regulations on occupational pension provision.

B. We recommend that the Inland Revenue give guidance on contribution levels normally allowable for the POP to avoid the danger of avoidance through overfunding, but that the tax treatment of the POP should continue to fall formally within the occupational pensions framework of limits on benefits (and hence permit accelerated accrual in appropriate cases). In this context the existing 15% limit on employee contributions may well become inappropriate if accelerated accrual has to be made in the period preceding retirement.

C. Although individualised schemes may aim to provide pensions related to final salary, they must be basically money purchase schemes. We believe they should be able to contract out of the State scheme if contribution rates are generous enough to enable the intermediary to satisfy the requirements of the Occupational Pensions Boards as regards Guaranteed Minimum Pension. We therefore recommend that the Occupational Pensions Board should not require that schemes contracted out also satisfy additional provisions for requisite benefits tied to final salary.

D. One current drawback to S.226 schemes is that they are restricted to insurance companies. This simplifies Revenue supervision. But it means that the net proceeds are subject to insurance company expense ratios and so it has reduced competition in this area and hence potential expertise and competition in the provision of individual occupational pension schemes. We recommend that the legislation be modified to allow bank trust companies and supervised intermediaries such as unit trust management companies and building societies to compete for S.226 and for POP business.

E. If individual provision is to offer as good pensions as pooled final salary schemes it is desirable that those who wish to do so can obtain full or partial protection against inflation. This means that a full range of maturities of index-linked securities should be available so that financial institutions are able to develop a market for index-linked annuities. We note that the Chancellor of the Exchequer indicated in his 1982 Budget statement that it was the Government's intention to continue to extend the range of index-linked securities. We recommend that when the Treasury reviews its funding strategy in forthcoming years it should take account of the usefulness of index-linked securities with a wide range of maturities in backing up individual pension provision.

F. One major disadvantage of individual pension provision has been the Revenue requirement that the accumulated fund (other than the lump sum) be wholly used to buy an annuity at retirement. This is one of the major objections to individual provision compared with pooled schemes whose continuing pensions are paid out of a fund whose performance can be averaged over the years. For the individual the date of retirement may coincide with depressed stock market values or depressed fixed annuity rates or, in extreme circumstances, both. The self-employed can avoid this problem by taking out a number of S.226 policies and crystallising them at different times. In Canada this is now proposed for all contribution-based schemes. We recommend that the Inland Revenue allow phased crystallisation of individual pension rights over a ten year period extending at least until age 70.

G. Improvement of individual provision through POP is likely to highlight the restrictions on S.226 provision for the self-employed and employees not in occupational schemes. The current limits on tax-exempt S.226 contributions of 17.5% (20% after 50) might be adequate for the person who makes provision throughout his working life, but are clearly inadequate for the more typical person who reaches 45 with low accrued provision and who therefore needs to accelerate his contributions in later life. We recommend that these limits should be increased as soon as fiscal considerations allow, with the particular priority given to the limits for those over 45 or 50.

H. Employees in pooled occupational schemes with inadequate accrued pensions cannot make individual supplementary provision through S.226 policies in respect of that employment; AVC schemes are the only vehicle available. We recommend that occupational schemes should have to make available AVC facilities as a condition of continuing tax approval.

I. Meanwhile the informed individual within pooled occupational schemes awaits the implementation of the 1981 Report of the Occupational Pensions Board on Early Leavers. We consider that the dimensions of the problem are becoming better understood within the pensions industry and that by 1984 a certain amount of action will have been taken voluntarily. However we consider that legislation will still be required and we recommend that in or about 1984 legislation be introduced to implement at least the minimum recommendations of the Occupational Pensions Board in respect of early leavers benefits accruing from the date of legislation.

36. If the Government took these actions then it could review progress within two or three years. It is desirable that individual pensions acquire their own momentum, especially within the occupations to which they are best suited, before further moves are made to affect the balance of the system.If the attractions of the POP were widely understood then it might be expected to spread because of employee pressure, whether individually or through collective bargaining. The measures outlined above might be insufficient to get the individual pension really moving. If it turned out that the current growth of AVCs combined with better treatment of early leavers satisfied individuals' needs, and that the POP had limited appeal to employees and could not be made to appeal without extra subsidies or tax-incentives, then it would be quixotic for Government to take further action in the face of the very real problems that are involved in the idea. However it might well be that individuals did want the POP but that employers were reluctant to concede it, and that they were supported in this by the minority of stayers, in senior management and trade union positions, who felt their interests threatened. In this case we recommend that the Government should consider legislating to give new employees the right to opt out of a pooled scheme. Similar provisions would apply to its own employees. To make this right fully

effective it might be necessary to compel employers to estimate for each employee the contribution deemed to be made on his behalf, to declare this to him, and to offer him the choice as to whether to invest this within a pooled scheme or individually; although it would be better if simple legislation was enough to allow an acceptable basis for the POP to be achieved through individual or collective bargaining. We recommend, however, that in the medium-term employers should retain the right to compel employees to make a specified level of pension payment; although when the habit of personal saving for retirement became more deeply ingrained, employees should be given the full measure of individual responsibility.

CONCLUSION: END OF THE PARTNERSHIP?

37. The current system of pensions provision is based on a partnership established under the Social Security Pensions Act 1975 between improved state provision, including SERPS, and good pooled final (or average) salary occupational pension schemes. The changes outlined above could lead in time to a somewhat different system. We consider that it would have positive effects on equity between pensioners, market flexibility and the visibility of pension arrangements; and more particularly, it would widen individual choice and increase the individual's perceived stake in profitable enterprise.

38. Many in the pensions industry are very concerned about proposals to make occupational schemes non-compulsory and to widen opportunities for individuals to make their own private provision. We can see why. If many employers chose not to impose minimum pension provision then it could lead to substantially less overall provision; and because much less of this pension provision would be contracted out the funded base of occupational pension provision could shrink enormously. The majority of the working population might have most of their pension needs met by the state, with a much smaller proportion being met by funded top-up. The choices open to the individual would have widened substantially; but the pensions industry would have to sell its wares to individuals as efficiently as to employers, involving far more transactions within a reduced aggregate business.

39. In practice we think that, although full implementation of the strategy outlined here would tend to reduce pensions provision, the net effect would be limited and therefore acceptable in the context of current concern about possible over-provision. We would expect the larger pension schemes, both public and private, to be able to satisfy most of their members that they offered a better deal than individual provision (through lower administrative costs, reasonable provision for early leavers, good investment performance etc). We would expect many of the smaller pension schemes to move towards a money purchase basis where individuals were given annual personal statements, and in a number of cases these would be topped up by final salary schemes for the minority of stayers.

40. The effect of this would be that pooled occupational pension schemes would remain the core of good private pension provision. However many individuals, e.g. middle managers, might opt for a POP in the first part of their career, and switch to a final salary scheme (if available) for their last ten to twenty years in employment. In naturally mobile occupations the POP might become the norm. And the fact of competition from POP should improve the visibility of all pension provision.

41. The increase in individual choice outlined would have the effect of relating a number of people more closely to the sources of wealth creation by individual commitment to policies or funds marketed by financial institutions. But it should not be assumed that it will lead to major reduction in the concentration of capital; and it might even increase it. Most people do not regard themselves as sufficiently knowledgeable to invest directly (except through house purchase). Even if they were they would get advantages in achieving a good return, combined with security, from pooling their savings with others in funds managed by a small number of large and well-respected institutions.

42. We believe that the measures outlined above are in principle desirable. But it is obvious that to achieve them all will require a cautious strategy to deal with the expectations, hopes and fears of existing and soon-to-be pensioners, as well as the well-articulated concerns of the pensions industry, and to ensure that the best of what has been achieved through compulsory employer provision is not unnecessarily eroded.

ANNEX

SOME OF THE PROBLEMS INVOLVED IN
THE PORTABLE OCCUPATIONAL PENSION(POP)

The level of provision (and hence of saving)

A1. It can be argued that the widespread adoption of the POP would be likely to reduce overall pension provision. We agree that pension provision could well become less attractive to employers than it currently is. Widespread availability of the POP would reduce the current bias against the mobile employee and so pension benefits would have a lesser role in rewarding loyalty. The employer would also have to meet the increased cost of fulfilling existing commitments to the stayers. And pensions would increasingly be seen by employees (quite reasonably) as a form of deferred pay rather than an apparent mark of employer goodwill and even philanthropy.

A2. We do not believe that many major employers would wish to dissolve their large pooled occupational pension schemes since these are now well established. However three processes could start to work:-

(i) on the assumption that SERPS continues, whether in its present form or modified, a minority of employers would take the view that the state, through SERPS, now provided a reasonable level of pensions for most staff, and that POPs could be negotiated for more senior personnel. These employers might choose to dissolve their schemes;

(ii) as set out in paragraph A16 below, a large number of smaller insured schemes might become insolvent if a significant number of people were able to opt out, and many of those schemes might be dissolved;

(iii) new growing companies, before they reached the stage when they would normally set up a pension scheme, would face demands from more senior and well-informed personnel for POPs and would be less likely to institute a pooled scheme for the remainder.

A3. Aggregate provision would then be likely to fall in two ways:-

(i) where employers with schemes offered choice without compelling a minimum level of pension provision, a large number of employees, especially new employees, would opt out, rely on SERPS and fail to make additional private provision. (Britain's largest private sector employer, GEC, already runs a voluntary scheme to which only one-third of its employees (half its male employees) belong, despite contributions of 7% offered by GEC to match contributions of 3% by the employee.)

(ii) many employees of smaller companies which dissolved, or failed to install, pooled schemes would not make equivalent private provision. In this case the most significant fall in prospective provision might well occur at junior and middle management levels where earnings are typically around twice average earnings. For these people SERPS represents a much less attractive alternative, offering about one-third income replacement to a married couple (wife not working). However, this group is not used to saving significantly for retirement and faces pressing commitments during most of working life to family, house-purchase etc. It is not likely -at least until the habit of saving became much more deeply ingrained - that this group would save as much for retirement privately as they now do compulsorily through pooled schemes. There would be a larger disparity between them and workers in the public sector and in private sector companies with continuing pooled schemes. However the more mobile among this group who did make individual provision could, if they chose, do substantially better than under the existing system.

A4. The reduction in provision would be less to the extent that employers remained concerned that they would face a moral obligation to those of their employees who had little beyond what the state provided in retirement, and therefore chose to continue to enforce a minimum level of contribution beyond the level enforced by the state. These employees would have the right to choose how to save, (ie through the company scheme or through a POP), but not whether to save.

A5. Leaving aside the question of incidence, a reduction in total pension provision might not be a bad thing. As we have suggested in "Pension Issues and Policy", the burden of pensions could become excessive in the next century if economic growth proves disappointing. A somewhat lower level of provision, coupled with greater choice about individual provision, might thus involve a more sensible balance between pensioners and the working population. In the shorter term it would also reduce employers' costs and hence be an aid to competitiveness and to the creation of employment. It should also involve some short-term Revenue gain, which might be set against the losses in tax that might flow from other reforms designed to aid individual pension provision.

A6. If, as suggested above, the number of occupational pension schemes fell, more people would participate in SERPS. Apart from other effects, this would reduce the amount of savings available for investment. However it is doubtful whether current levels of pension contributions represent an optimum level of saving for the UK. The substantial net cash inflow into pension funds (about £8bn pa) may not be fully matched by the availability of profitable opportunities in the UK, and part of it may simply be bidding up the price of eligible investments. On current projections pension funds will have a value (in terms of 1982 earnings) of £150bn by about 2020, compared to the current total value of UK quoted equities of £100 bn, and of UK government securities of £80bn. In any case most of this saving is actually or effectively compulsory. There would be no reduction in individual choice or disposable income if it was felt that this saving should be replaced by taxation or alternative forms of compulsory saving, but there would be an increase in choice if new methods of voluntary saving were developed instead.

<u>The Final Salary Promise</u>

A7. The second major problem of the POP is that it cannot <u>guarantee</u> a level of benefit which is related to final salary. There is a strong preference for final salary schemes among both employers and employees. It is regarded as desirable that incomes after retirement do not involve a significant fall in standard of living and final salary schemes are designed to this end. The alternative - contribution-based, or 'money-purchase' schemes - provide benefits which depend both on the contribution history and on the performance of the fund without the same level of guarantee as final salary schemes. The value of the fund can be eroded severely by inflation and by bad investment decisions in the period of accrual before retirement. The pension benefits can be eroded by inflation after retirement. Little of this is normally conveyed by those marketing money purchase or individual plans expressed in money terms.

A8. But in principle it is possible for people using contribution based schemes to overcome most of the problems and obtain something near the final salary promise. In the period leading up to retirement the state of the fund would need to be assessed at regular intervals and the contribution rate raised or lowered if the benefits seemed likely to diverge significantly from the target. Experience shows that, despite inflation, it is reasonable for a fund manager to assume a positive real rate of return on investments, over a lengthy period of accumulation. Trouble can however arise if inflation increases rapidly. The person near retirement might then receive large salary increases while the value of the funds underlying his pension would not grow enough to support a pension related to a target percentage of his retiring salary. To compound the problem, as retirement approaches, it would be normal practice to put the underlying funds in more secure investments which would be less likely to fall in money terms, but would also be less likely to keep up with or beat a rising inflation rate. Given time, the underlying fund would be likely to recover and possibly even to catch up in value, but the individual would suffer from having to crystallise the pension at an unfortunate moment. This problem can be partly overcome by allowing the individual to crystallise his pension over an extended period rather than (as now required by the Inland Revenue) at the time of retirement.

A9. A less frequent problem would occur where an individual near retirement received a substantial real increase in pay due to promotion; contribution rates could not then be increased sufficiently in the short time available to maintain a target pension. On the other hand under a contribution-based system the great majority of people who have a more even pattern of salary progression would no longer subsidise the pensions of those who are promoted close to retirement.

A.10 After retirement, there is no reason in principle why the holder of a POP need receive any less protection against inflation than the members of a normal occupational pension scheme. The individual can obtain protection by taking out an index-linked annuity supported by the availability of index-linked securities. However, so far there has been little or no demand for such annuities because the immediate income payable has been only half or so that achievable from fixed annuities. He can also take out an annuity which increases at a small fixed rate, or at a rate based on the performance of an underlying fund. In principle the lack of a full indexation guarantee means that these are better value for money. If POPs were to develop in competition with the better conventional occupational pension schemes it is therefore desirable either that index-linked securities with a wide spread of maturity rates should be made available to support index-linked annuities, or that the insurance industry should market more generally variable annuities to achieve an improved form of partial indexation.

The Actuarial Problem of Transition

A.11 The POP may be accepted as a desirable long-term goal, but there are severe problems of transition. From the individual viewpoint the prospect of opting out of occupational pension schemes is likely to appeal particularly to younger employees, both because they are more likely than older employees to foresee changes of employment which would make POPs attractive and, if pensions provision was voluntary, because they could spend the money on more immediate needs. The older employee is more concerned to hang on to the security of the pension provision which is more imminent.

A.12 The employer's contribution in many pension schemes, although usually presented as an averaged figure, is actuarially based on payments which vary with the age of the employee or his age of entry to the scheme. If the POP is to spread widely the pensions industry would have to develop agreed scales on which employers with occupational schemes could calculate equivalent contributions to be made to the POPs of employees who opted out of the company scheme. These scales would be based on age of entry, or actual age, depending on the structure of the scheme. More fundamentally, even actuarially correct contributions are not normally sufficient to pay for all the pension promises being made. It is assumed in the funding of schemes that large numbers will leave early, and the resulting reduced benefits will help to finance higher benefits for those who stay. If contributions were individualised, this unpalatable fact would become explicit to the individual employee.

A.13 None of this should present any problem to the employee, with accumulating skills and relevant experience, who is confident that he will be able to negotiate with prospective employers the right mix of pay and POP contributions actuarially appropriate to his age-range and hence achieve pension benefits commensurate with his salary progression. However many typical employees might be correctly advised that, once having opted out with small or nil employer's contributions, they will not be able to extract from that employer the much higher contributions after age 40 which would have to be made on their behalf inside final salary schemes. If they think of themselves as stayers, as most employees do, or if they are in schemes with good early leaver provision, then they will choose to remain within their final salary schemes.

A.14 For pension schemes the problem of transition would vary substantially. Many mature schemes, being strongly funded, would have no problem if they lost many of their younger members. Even if there was a loss of contributions from younger employees and from new entrants, and the employer's contribution rate increased for those who remained, this would actually represent a lower total cost, thus providing scope for significant employer's contributions to POPs.

A.15 However there is a large number of schemes which increased benefits in the early to mid 1970s on the basis that they would be funded over 8-15 years. Some of these schemes will depend for a few years longer on contributions from younger employees to finance benefits being paid to those who have recently retired or are to do so shortly. The Government is in a similar position indefinitely with regard to the pay as you go scheme for its own employees. A POP option for them would involve a short term Exchequer cost.

A.16 Finally there are schemes whose contribution levels do assume continuing new entrants. Many insured schemes are of this type. If the flow of new entrants paying contributions were cut off then the scheme would require higher aggregate contributions which could only be paid by the employer or the remaining employees. If the employer sought to share this burden with the remaining employees, this would lead to further withdrawals and probably the dissolution of the fund.

A.17 No information is available on the proportion of schemes which is in each category. The pensions industry has an interest in maximising its assessment of the disruption that individual choice would cause. The Government as employer, and paymaster for the public sector, has a similar financial interest in schemes. It is however clear that if the question of individual choice is to be pursued, further work would be needed to quantify the number of pension schemes which might be at risk of significant increases in aggregate contributions by employers and older employees to maintain current benefit promises. Our own view, based on discussions with individuals in the pensions industry, is that individual choice would pose no insuperable problem for the better and larger occupational schemes, but that a large number of smaller, generally insured, schemes could be at risk. This means that the spread of POP would bring pressure on smaller schemes but that final salary schemes would remain available for those who preferred them in most large organisations.

The Administrative Problem

A.18 Pooled schemes are a cost-effective method of providing pensions. Administrative expenses can be as little as 3% of contributions in large schemes. In contrast individual pension provision causes administrative problems to the employer if he is involved in it, as well as bringing in an outside body - the insurance company or other intermediary providing the scheme - with its separate administrative structure. This could be simplified for employers if they negotiated preferential terms with (say) three intermediaries; the greater the extent of concentration the less costs would differ from those in pooled schemes. Employers might also be able to impose contributions rates based on actuarial advice which would also be limited by the Inland Revenue to prevent overfunding, subject to facilities for those over 50 to vary the prescribed contribution rate. None of this is very different from what happens when companies offer the facility for Additional Voluntary Contributions (AVCs) to be made to an insurance company or building society. The cost is partly taken by the employer in computer and personnel costs, and partly by the individual in the return offered by the intermediary.

A.19 The administrative problem becomes very different if the employer faces individualised contribution rates and a large number of intermediaries. This full exercise of individual choice would have substantial costs. These would have to be met by reducing the individual's benefit, although the costs would still be less for many than the penalties they suffer under the existing system. However it is essential to the concept of the portable pension that the new employee, when joining, should be able to bring his pension with him and to maintain his contributions with the pensions intermediary (albeit at a cost).

A.20 If a restricted choice of intermediaries was preferred on cost grounds then there should be machinery for fair transfer of accrued pension rights between intermediaries. Alternatively and very much a second best, these rights would be preserved (as now within a pooled scheme) and the 'portable pension' for a mobile employee would in fact consist of a lifetime's collection of pension rights.

A.21 Administrative complications should be containable for the Inland Revenue if a limited number of intermediaries (insurance companies, pensioner trustees and certain others) continues to be authorised to act for the Revenue in ensuring that total employee benefits are limited to those allowed for occupational pension schemes. Even on this basis individual pension provision obviously imposes some extra staff costs. If this was thought to be excessive a small charge for approval might allow this to be recouped.

The Problem of Benefits on Death and Early Retirement through Ill-health

A.22 An advantage of pooled schemes for both employer and employee is that they offer benefits on death during employment and pensions payable on early retirement through ill-health. Life insurance can be purchased individually, but some employers might feel the need to compel this provision to avoid claims to support widows and other dependants. Individual insurance against early retirement through ill-health is less usual. Permanent health policies are however now available under some S226 contracts, and would be likely to become more widely available if the POP became widespread. This still leaves the problem of self-selection against a pooled scheme, ie that those who remain would be the less healthy; this is an inevitable consequence of a reduction in cross-subsidisation and carries a cost, payable by them or by the employer.

CONFIDENTIAL

cc RPM

Copy No 1

PENSIONS ISSUES AND POLICY

A Paper by the CPRS

April 1983

CONFIDENTIAL

CONTENTS

CONFIDENTIAL

This paper indicates that its authors have no idea how to tackle a problem of this kind. It recommends policies as far apart as A & Z. In politics you can only at most go from about A-D at a time. Moreover it is and would be seen to be absolutely disastrous if it were to go any further? I reject it, MT

PENSIONS ISSUES AND POLICY

SUMMARY

1. In autumn 1982 the CPRS undertook to review the future of pensions provision within the context of other Government objectives (eg improving the performance of the economy, increasing people's stake in profitable enterprise and widening individual choice).

2. Work by officials is currently in hand on a number of pensions issues such as the burden of pensions, possible changes to the new state scheme in the light of the 1982 Quinquennial Review of the National Insurance Fund, pension contributions and Civil Service pay, the Government's response to the Social Services Committee's recommendations on the age of retirement, and questions on disclosure by occupational pension schemes, on trust law and on supervision following recommendations in September 1982 by the Occupational Pensions Board. In addition, there is continuing interest in the problem of early leavers and the implications of the growing volume of funds accumulated by pension funds.

3. Ministers will need to have clear objectives and a co-ordinated strategy for dealing with the various issues. We suggest as main objectives (para 17):

- to encourage saving for retirement and a self-reliant and responsible approach to retirement saving.

- to improve the range of opportunities for retirement saving. ?

- to ensure that the social security system prevents poverty in old age.

- to encourage a system of pension provision in which pension promises are affordable and adapt smoothly to the underlying growth of the economy.

- to encourage the development of a pension system which is consistent with the desirable evolution of the economy.

4. But there are also constraints which could affect action to pursue the main objectives (paras 19-22):

- in the 1970s a broad consensus emerged between the political parties about the role of the state pension and the partnership between the state and the occupational pension movement. This consensus might not survive radical reform of pension arrangements.

- pensioners are currently seen by the public as one of the most deserving sections of the community. This might well cease to be true when the full burden of present pensions commitments becomes clear and its impact is felt by the working population. But the Government needs to act now to avert future problems, even if they are more than 20 years away.

- even existing commitments on pensions could outstrip the growth of resources to pay for them. This might mean that the cost of any improvements in pension arrangements would have to be offset by other changes.

5. The objectives, if adopted, would have important implications for pensions policy (paras 23-54):

- the aims of the National Insurance pension scheme and the role of the state would need to be reviewed. We indicate that the existing scheme is not a cost-effective way of achieving one of its main aims: reducing the dependency of pensioners on means-tested benefits (paras 26-32).

- we note also that the introduction of an earnings-related state pension (a component of the compulsory National Insurance pension scheme) is intended to compensate for some of the deficiencies in other pension arrangements (occupational schemes and private savings). But the extension of state involvement into earnings-related pensions is difficult to reconcile with an aim of encouraging individuals to be more self-reliant when providing for their retirement. An alternative approach would be to tackle the deficiencies of (non-state) pension arrangements directly and to reduce the state's involvement in the provision of earnings-related pensions. The social security system (including the National Insurance pension) would aim to prevent poverty in old age. More of the responsibility for pension provision above the poverty level would be placed on the individual (paras 33-35).

- we suggest that options now under consideration by officials for reducing the earnings-related element of the National Insurance pension scheme could be balanced by improvements in benefits aimed to buttress the state's role in preventing poverty in old age. Such a package could be designed to secure long run expenditure savings, although there might be extra costs in the shorter term (paras 36-38).

??

- Ministers should approach with extreme caution the Social Services Committee's proposals for changes in the retirement age. These could lead to very expensive additional burdens for the future without being a particularly cost-effective means of relieving current unemployment. But we see the benefits of a more flexible retirement age and suggest a way of achieving them (paras 39-42).

- if individuals are to be more responsible for pension provision above a floor set by the social security system, there is a need to improve people's understanding of their financial needs and responsibilities and to widen the opportunities available for tax-efficient, inflation-proof retirement saving (para 43-45).

- in view of worries about the cost of pension provision, certain desirable improvements in private sector occupational pension schemes, eg in benefits for early leavers and in protection of pensions against inflation, could be afforded if there were a cut in the level of pensions which schemes promise to pay in relation to final salary (para 46). Any changes in occupational pension schemes which leave some people worse off will be hard to achieve, but we propose a number of steps towards reform. Actual and perceived disparities between benefits offered by public and private sector occupational schemes could be reduced (paras 12 and 50). The visibility of pension arrangements could be improved through disclosure and other means. Members of schemes would then be better able to understand the reality behind the pension promises made to them and to take a closer interest in the efficiency of pension fund performance (paras 51-52). Measures could be introduced to facilitate competition and choice between different types of occupational pension scheme. We suggest widening the scope for individual, portable pension schemes (paras 53-54 and a companion CPRS paper "Pensions and Individual Choice" which examines the possibilities in more detail).

ACTION (paras 55-57)

6. We recommend that Ministers should first review their objectives. This could mean, in particular, redefining the role of the state. Then the various options for change, some of which we have identified, should be examined. The results of current official work will help with some of these. A major part of the background for decision is the risk of an excessive burden of pensions in the longer term. The temptation to ignore the potential future burden will be great but should be resisted, if it is not to become harder to deal with. In addition to the work already in hand, we suggest three further topics for study:

(a) The costs and implications of the various ways of preventing poverty in old age while reducing the earnings-related element of the state pension scheme.

(b) Measures to reduce disparities in pension provision as between public and private sector occupational schemes.

(c) Reform of the tax treatment of retirement and other savings and of pensioners' incomes.

PENSIONS ISSUES AND POLICY

INTRODUCTION

1. Pensions policy is a wide and complex area, and many important issues lurk within it. Have we set up a pension system that, ultimately, we shall not be able to afford? Are people encouraged to be self-reliant and save as they think best for their retirement needs, or is the whole system weighed down by the paternalism of the state and of corporations? Do the anomalies and inequities within the present system matter? And what is the impact of the pensions system on the development of the economy - for example on labour mobility, enterprise, and the working of capital markets?

2. Several important pensions issues will be coming to Ministers over the coming months. Many of these issues which will be considered separately are interrelated and cannot be sensibly settled in isolation. In this paper we:

(a) map out some of the more important issues and their interconnections;
(b) suggest some objectives that Ministers might have in mind for pensions;
(c) outline some of the practical implications for pensions policy.

Our intention is not to draw up full prescriptions for reform. These can come only after Ministers have decided their objectives and considered the results of current and further work by officials.

MAJOR CURRENT ISSUES

3. Although not exhaustive of the full range of issues relevant in the world of pensions, those matters shortly to come to Ministers' attention are substantive ones. The following paragraphs provide a conspectus.

The Burden of Pensions

4. This is one of the most important areas of concern - have we a pensions system which will impose an intolerable burden on the economy in the future? An interdepartmental group of officials, DHSS led, is looking at this, but some general points can be made at this stage:

(a) We need to examine the impact over the next 50 years of the rise in pensioners' incomes from all sources, in particular, occupational pension schemes and the National Insurance state pension scheme, introduced in 1978, which provides an earnings-related pension in addition to the basic flat-rate state pension. Occupational and state schemes aim to redistribute resources from people's working lifetime to their own retirement. Both result in a transfer of resources from workers to pensioners in the sense that resources consumed by pensioners are not then available for consumption by the working population. Rising rates of National Insurance contributions are an important element of the transfer problem.

(b) Such a transfer, if it implied little or no improvement in the real living standards of those in work, could well prove unacceptable and so inflationary and economically damaging. What is crucial therefore is the underlying growth of productivity in the economy. With reasonable productivity growth, very large transfers to pensioners could be consistent with continued growth in the real incomes of those in work. With poor growth, however, increased pension expenditure could create economic and social tensions as (unproductive) pensioners appeared to gain relative to a not particularly affluent working population.

(c) On the basis of present commitments*, there will be some increase in the global amount spent on pensions over the next 20 years or so. The major growth of expenditure however will occur in the next century. Total pension expenditure should then grow substantially, both in absolute terms and in relation to wage incomes. These developments over the next 50 years partly reflect movements in demography - favourable until the early part of the next century as the numbers of working age rise relative to the number of pensioners, but rapidly deteriorating thereafter as the relatively large population born between 1946 and 1970 retires. In addition, average pensions are projected to rise relative to average wages largely because of the increase in earnings-related state pensions, as the new state scheme matures, but also because of better occupational pensions resulting from the delayed effects of past improvements.

(d) Although, in aggregate, pensioners should be very well provided for in 40-50 years time, many pensioners could remain in need over the next 20 years or so. Earnings-related payments under the new state scheme will build up gradually but the first full earnings-related pensions will not be made until the end of the century. It will take many more years after that before the full liabilities of the state scheme are realized. The earnings-related element of the state scheme is of little if any benefit for the vast majority of existing pensioners who have retired with little or no earnings-related state entitlement. Currently, out of around 7 million pensioner households

---

* Here and elsewhere, "present commitments" are taken to include the uprating of the basic state pension in line with earnings, a provision which, with real growth, is more generous than the legal minimum requirement for uprating in line with prices. Historically, the basic state pension has been uprated to a level around a fifth of average male earnings and any progressive reduction in this level could prove unsustainable in the light of its effect on relatively poor pensioners. Ministers have expressed the intention of increasing benefit rates by more than the minimum provision when economic growth is restored.

there are 1.7 million households receiving means-tested supplementary pensions. It is estimated that half as many again are eligible for supplementary benefit but do not take up their entitlement. We therefore face the prospect for many years to come of having large numbers of (increasingly elderly) pensioners dependent on means-tested benefits. And even after that, when the new state scheme is fully mature, a number of pensioners, particularly those low paid in working life and not covered by an occupational scheme, could still be relatively poorly provided.

(e) The position of pensioners this century with no significant state earnings-related entitlement is likely to give rise to persistent demands on the government of the day to make better provision for them. One way, which would not add to long term commitments, would be to credit-in existing pensioners on a selective basis to the state earnings-related scheme. In addition, there could well be other pressures for change both in this century and in the next:

- earlier retirement;
- improvements in preservation and indexation of private sector occupational pensions;
- an increase in the basic state pension to boost the pensions of the low paid with little earnings-related entitlement;
- improvements to the earnings-related element of the new state scheme, for example, enabling contributors to build up increased earnings-related pensions over more than just 20 years.

Unfavourable demographic developments - a continued low birth rate for example - could also add significantly to the number of dependent pensioners per head of the working population. All these factors can only increase worries about burden based on the projection of costs of existing commitments.

(f) In short:
- over the next 20 years or so, many old pensioners remain in risk of poverty unless their state pension is improved;
- in 50 years time, if not earlier, there is a risk of an excessive burden of pensions, with adverse social and economic consequences.

State Pension Scheme

5. Officials' work on the burden of pensions will inform another interdepartmental group, DHSS led, considering possible important changes to the new state scheme. The remit of this group, formally set up in response to the Government Actuary's 1982 Quinquennial Review of the National Insurance Fund, concentrates on reductions in state pension commitments and does not embrace other sources of retirement income. The group will focus on various aspects of the earnings-related component of the state scheme which have the effect of favouring certain groups - in particular, current middle-aged workers and women. Cutbacks in earnings-related entitlements could help lighten the pension burden but would hardly be politically attractive. Should Ministers nevertheless decide upon any reductions in entitlements, they might prefer to include them in a more comprehensive package of reform containing elements to make the reductions more politically acceptable as well as socially and economically desirable.

Retirement Age

6. With the prospect of high levels of unemployment at least in the short term and, as a result, falling labour force participation by older workers, Ministers will continue to be faced with pressures to lower the age of retirement, either selectively or generally, as a way of reducing the number of unemployed. In particular, there will be a need to consider whether Special Employment Measures involving early retirement eg job release, should be retained, converted into permanent arrangements or abandoned.

7. In addition, the Government will shortly have to respond to proposals made by the Social Services Committee, in its 1982 report on the Age of Retirement, that, on grounds of equity and freedom of choice, there should be a common retirement period for both men and women from 60 to 65: the full pension should be payable at age 63 (instead of 65 and 60); people retiring earlier than 63 should receive an abated pension while those retiring later should receive an augmented pension. These changes should be phased in by 1998 at the latest.

8. The Committee indicates that a common retirement age of 63 would cost over £500 m a year in extra public expenditure (after allowing for Exchequer savings on unemployment-related benefits including supplementary benefit) and might increase the cost of occupational pensions. In fact, the full costs could be a lot higher (see paras 40-41 below). The Committee did not regard their proposals as deserving first call on any extra resources for pensions. They put improved pensions for existing pensioners at the top of the list.

9. In "Growing Older", published in 1981, the Government expressed its general support for a common flexible retirement age, subject to constraints on resources.

Public Sector Pensions

10. Occupational pensions in the public sector present a series of difficult problems. On the one hand, inflation-proofing of pensions in payment, transferability and usually full preservation of pension entitlements on changing employers within the public sector transfer club are regarded as characteristics which would be desirable in a reformed occupational pensions system for members in both public and private sectors. On the other hand, to extend the public sector model - the Rolls Royce of the pensions world - to the bulk of the population could be prohibitively expensive (though some occupational schemes in the private sector already offer excellent benefits). Policy aimed at reform of the occupational pension system has to perform the difficult trick of reducing the perceived disparities between pension provision in public and private sectors, while, at the same time, neither losing the best features of Rolls Royce engineering nor adding excessively to the pensions burden if the economy can afford only a Maestro.

11. To date, attention has focussed on the cost of inflation-proofing public sector pensions - the subject of the 1981 Scott Report. Ministers have indicated that one approach might be to make pensions contributory, which is in line with the recommendation of the Megaw Report on Civil Service pay, now under consideration in MISC 83/84.

12. With the fall in inflation, attention in the pensions world has switched to the absolute level and quality of public sector benefits in retirement. Two particular issues have emerged:

(a) Integration

In most public sector schemes, the pension benefit formula takes little account of the flat-rate basic state pension but in the larger private sector schemes the pension is commonly abated by a process of "integrating" the occupational pension with the flat-rate (and sometimes the earnings-related) state pension. Although there would be difficulties in achieving integration in the public sector and adjusting contribution rates accordingly, integration would reduce the risk of "over-pensioning" in the public sector with employees being better off in retirement than in work and would be an example for those private sector schemes which are not fully integrated.

(b) Security

Pensions in the public services have the security of the Exchequer (or ratepayer) behind them. In the nationalised industries the position is more confused. Certain pension schemes such as British Airways carry a solvency guarantee which effectively gives ultimate recourse to the Exchequer. In others, such as British Rail, the level of pension contributions payable by employer and employee (and ultimately of benefits) is determined by the performance of the pension fund. Parity of treatment with the private sector would require the wider adoption of the British Rail model, especially in the nationalised industries, thereby removing a presumption to an Exchequer guarantee.

Disclosure, Trust Law and Supervision

13. In September 1982 the Occupational Pensions Board (OPB) made a number of recommendations on disclosure by occupational pension schemes, and the principle of legislation to enforce adequate disclosure was immediately accepted by Ministers. Disclosure will apply to the financial arrangements of schemes including information on their assets and funding status. A Working Group of officials led by DHSS is considering implementation. The group is also considering two other matters:

(a) whether trust law provides an adequate framework for modern pension funds or whether it should be replaced (a question raised by the same OPB Report); and

(b) whether supervision of funds by an official body is desirable, and if so in what form (questions prompted by concerns about the position of pension funds, the supervision extended over other savings institutions and the failure of self-regulation at Lloyds).

14. In considering what action to take on these matters, the official group will distinguish between the aims of giving pension scheme members greater security than they now have, and of ensuring more openness in the operation of pension funds. The latter would improve public understanding about pension funds, the conditional nature of the promises they make, and the dependence of pensions on the success of the economy.

15. This list of issues of current concern is clearly not exhaustive. Other pressing worries about the evolution of the pension system include:

(a) Early Leavers

Despite improvements in preservation rights following pension legislation in the 1970s and the decision of Ministers to remove a technical abuse ("franking") of the new state pension scheme, mobile employees will continue to be penalised by present arrangements in private sector occupational schemes. In view of the implications for company costs, Ministers decided not to give immediate legal backing to the OPB's 1981 recommendations on "early leavers" (ie employees who cease to be serving members of a particular occupational scheme before normal retirement age for reasons other than death or early retirement on pension). Currently, there is renewed interest in stimulating "money purchase" pension arrangements in which benefit entitlements are defined by the record of contributions, as in a personal savings plan. Money purchase pension schemes, either on top or in place of final salary occupational pension schemes, provide the employee with individual rights and thus a pension which can be portable between different occupations.

(b) Pension Funds

The market value of the assets of pension funds, including those invested through life assurance offices, is now probably about £120bn and, in real terms, could triple over the next 50 years. This prospect adds to concerns about the concentration of ownership of financial capital - and thus exposure to political direction - and the effect on investment rates of return in general and the impact on particular investors (eg small innovative firms). Doubts are raised about the scale of the tax concessions to pension funds which are more favourably treated than other channels of saving.

OBJECTIVES AND CONSTRAINTS

16. In order to construct a pension policy within which these and other issues can be coherently resolved, the Government needs to be clear about its objectives and to recognise the constraints it faces.

17. The development of a consistent set of objectives will be an evolutionary process as Ministers review the current pension system and consider in detail the implications of alternative goals. At this early stage, we can offer only a preliminary and general list of main objectives which Ministers might hold:

(a) To encourage saving for retirement by a regime - not necessarily the present regime - of tax incentives. The nature of these incentives will depend in part on Ministers' long term objectives for the tax system as a whole.

(b) To encourage a self-reliant and responsible approach to retirement saving: a major departure from existing practice. This will involve improving individuals' awareness and knowledge of pension arrangements, simplifying these where possible and reducing state and corporate paternalism in the form of compulsory pension provision.

(c) To improve the range of opportunities for retirement saving in a way that does not discriminate unfairly between individuals according to, say, their occupation, their income, their sex or their preferred method of saving. A policy of encouraging self-reliance would ring hollow if pension arrangements were allowed to favour unduly some sections of the community at the expense of others.

(d) To ensure that the social security system (including the National Insurance state pension) prevents (relative) poverty in old age and is financed in a way which is consistent with objectives to relieve (relative) poverty, while retaining work incentives, in working life. In particular, the National Insurance state pension should not be dependent on impossibly large contributions from the low paid.

(e) To encourage a system of pension provision in which pension promises are affordable and adapt smoothly to the underlying growth of the economy. Active members of pensions schemes could, with advantage, be made to understand better the link between economic performance and their own living standards in retirement.

(f) To encourage the development of a pension system which is consistent with the evolution of more flexible and responsive capital and labour markets. The more impediments to growth are removed, the greater the chance that the nation will be able to sustain, inter alia, a generous level of pensions. Ideally pension arrangements should not reduce work incentives, nor retard wage adjustment; they should constrain neither labour mobility nor the evolution of flexible patterns of working time; and they should not inhibit the development of smaller scale, dynamic enterprises nor "clog" financial capital markets.

18. The main constraints acting on pension policy are described in the following four paragraphs.

Political

19. The present compromise between the political parties on the role of the state pension and the associated partnership between the state and the occupational pension movement were reached after years of hard and sometimes disruptive debate. The political consensus included the aim that the individual's total pension, whether provided by the state or by occupational schemes, should be above the supplementary benefit level. At the very least a continuing consensus is important if, in a climate encouraging greater self-reliance, people are expected to plan sensibly and save for their retirement needs. If stability is highly valued, it will be impossible to abandon completely the present arrangements for state earnings-related pensions even though they conflict with other important objectives eg 17(b) above. Less radical but desirable reform is not, however, necessarily ruled out if Ministers decide that they wish to preserve a political consensus.

Public Perceptions

20. Pensioners are seen by the public as one of the most deserving sections of the community. Government action, even if designed merely to pull back future benefits that nobody is currently enjoying, could be misrepresented as an attack on the poor. The fact is that, in the next century, the elderly will on average be well provided for. But today's perceptions will make it difficult to solve the day after tomorrow's problems. And in the field of pensions, solutions cannot be long postponed.

Economic

21. There will be continued pressure for often expensive reforms of the pensions system but whether reform should be undertaken at all and, if so, with what priority depends on the availability of resources. Officials' work on pension burden suggests at least a need to avoid adding to existing pension commitments unless the proposed improvement is of the first importance. Other desirable reforms would be acceptable if based on a reallocation of committed resources rather than net additions.

22. If Ministers come to regard present commitments as excessive, they will probably have to alter pension arrangements now, so as to avoid building up future entitlements. Such cutbacks might concentrate on those sections of the pensioner population likely to be best provided 50 years hence lest an across-the-board reduction precipitate a number pensioners who are then relatively poorly-provided into poverty. Though it will always be technically possible to tackle an excessive pension burden at the time - eg by de-indexing benefits then in payment - such adjustments so late in the day are likely to be economically and socially disruptive. Moreover, adjustment, while technically feasible, may prove to be very difficult politically. The historical anachronism of the lower retirement age for women provides a vivid illustration of how much easier it is to confer a benefit than it is to take it away.

IMPLICATIONS

23. If these objectives and constraints are accepted they have important implications for a number of the issues with which Ministers will shortly be faced. In the following paragraphs, we outline some of the main points.

The Role of the State

24. The need to review the role of the state and, in particular, the aims of the state pension scheme arises as a result of the work on the burden of state pensions (paras 4-5) and the related requirement to implement any changes before strong expectations of new entitlements have built up.

25. When the new state scheme was introduced, it had two main aims:

(a) to prevent large numbers of future pensioners having to rely on means-tested benefits: the National Insurance state pension had therefore to cover at least basic needs; and, beyond that

(b) to protect an individual, on retirement, from a severe decline in his living standards: the state therefore took on the responsibility for providing a certain level of "income replacement" in retirement (ie the pension replaced a proportion of previous wage income).

The scheme also had other important but subsidiary aims including those of establishing a partnership between occupational pension schemes and the state, of increasing provision for widows and of improving labour mobility. It is worth examining the rationale for the two main aims in turn.

Aim 1 : Covering Basic Needs

26. As earnings-related entitlements build up, and as poor pensioners with little or no earnings-related state entitlement or occupational pensions die, the number of elderly recipients of means-tested benefits will fall. The new state scheme will therefore fulfil the first aim, given time to develop to maturity. The use of a selective (means-tested) benefit like the supplementary

pension which directs resources to those most in need is of course more cost-effective than a universal benefit like the National Insurance state pension. However, a system of means-testing is seen by some as socially divisive, detrimental to self-respect, self-reliance and thrift. The system is costly to administer and subject to poor take-up. Even though the general balance of advantage as between universalism and selectivity is debatable, supporters of the new state scheme believe that pensioners at least should not be stigmatised by having to rely on the charity of means-tested benefits in order to keep themselves out of poverty.

27. The fact remains however that, seen simply as a way of floating pensioners off means-tested benefits, the new state scheme is very costly. It relies almost entirely on the earnings-related element to improve pensioners' incomes. And with earnings-related benefits, an important proportion of the extra expenditure will inevitably go to higher income earners, and so take their pensions above, perhaps well above, a minimum level of income necessary to cover basic needs.

28. No comprehensive estimates are available of the proportion of state pension expenditure which will in the future go to pensioners with different levels of retirement incomes, apart from their state pension. Calculations can, however, be made to show what size of state pension a single man with a full record of National Insurance contributions could receive on different assumptions about his earnings throughout his working life (see table below).

SINGLE MAN'S PENSION (WITH FULL ENTITLEMENT IN NEW STATE SCHEME)

Earnings (throughout working life)	State Pension (per week, rounded figures)
½ national average	£45
national average	£66
1½ times national average	£83

Notes

1. For illustrative purposes, average national male pay taken to be £165 per week.

Notes to table (continued)

2. Pensions based on April 1983 levels of benefit and National Insurance earnings limits. The single person's basic flat-rate pension is £32.85 a week.

3. The full earnings-related component of the state pension is equal to a quarter of average qualifying earnings (ie earnings lying between the National Insurance limits) in the best 20 years in a working lifetime. Pensions at the level shown in the table could be paid after 1998.

It is for Ministers to judge how such state pensions relate to a notion of a reasonable minimum level of income. But it does seem likely that many pensioners would be receiving state pensions well in excess of supplementary benefit levels.

29. There is a further issue. It is sometimes thought that the benefits of the new earnings-related component of the state scheme will go largely to those without reasonable occupational pensions and that little or no extra public money will go to those in good occupational schemes. This is not so. Quite apart from the fact that there are some good occupational pension schemes (eg John Lewis, GEC) which have not contracted-out of the new earnings-related component, 90 per cent of members covered by occupational schemes which have contracted-out will also receive substantial benefits from the state.

30. Contracting-out does not alter a pensioner's entitlement to the inflation-proofed earnings-related component of the state scheme. It merely alters the source from which the payments are made. The contracted-out pensioner will get part of this component (the so-called Guaranteed Minimum Pension - GMP - the level of which is determined by the state) from his own occupational scheme. He will receive the rest from the state. The GMPs received by members of contracted-out schemes will usually be smaller than their entitlement to the earnings-related component of the state pension. This is in part because of the way in which the entitlements to the GMP and the entitlements to the earnings-related component as a whole are calculated and in part because it is the state and not the occupational scheme which pays

the cost of the price indexation applying to the whole of the earnings-related component. The gap between the cost of GMPs and the earnings-related entitlements of members of contracted-out schemes will be limited during the early years of the scheme but widen appreciably as it matures.

31. Assuming 8 per cent annual earnings growth and 7 per cent annual prices growth (ie about 1 per cent annual productivity growth), figures from the Government Actuary show that annual state pension expenditure could ultimately* amount to £25 bn at constant 1981/82 earnings. Of this, £15½ bn will go to recipients of the flat-rate basic retirement pension and £9½ bn to those entitled to the additional earnings-related component. Of the £9½ bn state expenditure on the earnings-related component, £4½ bn will go to those not contracted-out (including, as indicated above, members of some good occupational schemes) and £5 bn will go to the members of contracted-out occupational schemes who on average are likely to be among the better paid members of the population. (Note also that they will be receiving from their own schemes GMPs worth just over £2 bn a year, representing about 30 per cent of their full earnings-related state entitlement.) With lower productivity growth but similar rates of earnings inflation, expenditure on earnings-related pensions would be higher as would be the proportion going to contracted-out members, and conversely.

32. Against this background, it is clear that the new state scheme will, when mature, fulfil the aim of substantially reducing pensioners' dependence on means-tested benefits, but it does so in a cost-ineffective way. The full state pensions payable may in many cases be well above that necessary to float pensioners off supplementary benefit. Substantial sums of public money, raised through the National Insurance system, will be spent on providing state earnings-related benefits for members of good occupational schemes. It should not be forgotten that existing pensioners, unless in receipt of an occupational pension, have to rely largely on the basic, flat-rate state pension.

---

* The "ultimate" position refers to a time when (a) the total population of the country is stable and (b) the full liabilities of the new state scheme have been realized. Although conditions (a) and (b) may never be met precisely, for practical purposes, the "ultimate" could be thought of as a position reached towards the middle of the next century.

Aim 2: Income Replacement

33. The case for the state pension in its present form largely rests on the second goal, which it achieves, of providing a certain level of "income replacement" via earnings-related state pensions. In the pensions debate that went on throughout the post war period, it was argued that the state should provide comparable benefits for those whom the non-state system - principally the occupational pensions schemes - failed. The limited and variable coverage of occupational schemes, their reluctance to index pensions in payment or to dynamise preserved benefits, the alleged improvidence and/or ignorance of individuals with regard to their retirement needs and the damaging effect of tax and inflation on the scope for individual saving were seen as factors which required further state intervention. This eventually came in 1975 with the passing of the legislation which provided for the new earnings-related state pension scheme.

34. Despite the acknowledged deficiencies of the existing non-state pension system, this rationale for the state's involvement in income replacement gives little weight to personal freedom of choice. The extension of the role of the state into compulsory earnings-related pensions is paternalist. The new state scheme imposes a universal pension regime (though the mechanisms differ for those "contracted-in" and those contracted-out). Workers with the same pay will be compelled to make contributions and then receive identical earnings-related state pensions (including any GMPs). This regime therefore largely ignores individual preferences regarding the level, timing and form of retirement savings. Private markets are potentially better placed to cater for a wide variety of retirement plans - including irregular retirement saving or the building up of personal assets (including housing) with a view to subsequent encashment. In defence of compulsion, it is sometimes argued that the individual's savings decisions are inherently irreversible and that people often regret the improvidence of youth. But such irreversibility can cut both ways: those forced to be thrifty may later regret the loss of opportunity of spending more of their income while young enough to enjoy it.

35. Had high priority been given in the 1960s and 1970s to the objective of promoting individual liberty and self-reliance, the appropriate response to the perceived inadequacies of the non-state arrangements for providing retirement incomes would not have been to compensate by extending the compulsory state pension scheme. Rather, the best response would have been to tackle the deficiencies of the non-state pensions system directly (discussed in greater detail below). Implemented successfully, this approach would have left the state with the important role of preventing poverty in old age (objective 17(d)). There would have been no call for an earnings-related state pension, nor a need for contracting-out arrangements.

36. The reality, however, is that these now exist. Ministers will wish to consider the case for complete abolition of the earnings-related scheme, although the political difficulties of doing so seem very large. Even if Ministers reject complete abolition, the factors we have mentioned do, we believe, indicate the direction of reform when Ministers come to review the options for reductions in the earnings-related element of the state scheme now being considered by officials (para 5 above).

37. Ministers might, for example, wish to consider a rounded package of measures. Cutbacks in the earnings-related state pension, because of worries about pension burden and/or paternalism, might be balanced by improvements, implemented perhaps during the next parliament, which would help those more in need - especially groups of pensioners now or in the future likely to be dependent on means-tested supplementary benefits. Increasing benefits for existing pensioners while cutting back on earnings-related entitlement could in the long run save money, and would have the presentational advantage of being immediate and thus more visible than the longer term losses of benefits. Such a package is likely to involve additional net expenditure in the shorter run compared to present commitments. But this comparison may be unrealistic. For, with present arrangements, there will be in any case mounting pressure to compensate existing pensioners as more and fuller earnings-related entitlements build up under the new scheme (see para 4(e) above).

38. Further work by officials will be required to establish the costs, advantages and disadvantages of options for improvements. These need not be mutually exclusive. Options include:

- adding to the basic flat-rate retirement pension in a selective (but not necessarily means-tested) way to benefit those groups most at risk of falling into poverty (eg older pensioners, retired widows or those without significant earnings-related state entitlement). It would be necessary to examine the extent to which such benefits accrued to those who already had adequate incomes. Such "leakage" would however be less than if the basic flat-rate pension were raised for everyone.

- raising the basic pension universally would also deserve consideration if it proved more cost-effective in preventing poverty than the existing earnings-related component of the state scheme. It should be noted in this context that, as a result of the introduction of Housing Benefit, many of those now eligible for supplementary benefit will be left with very small awards and it should be possible to float large numbers of pensioners off supplementary benefit by a comparatively small increase, selective or universal, in the basic pension. A universal increase in the basic pension would face two particular difficulties. In the past, attempts to raise the basic pension relative to supplementary benefit have proved difficult politically. But this difficulty might be surmounted if the same index were used to uprate both the basic state pension and supplementary benefit and if, from time to time, the basic pension were given separate and additional increases. Secondly, the retention of earnings-related contributions if flat-rate state pensions are increased and earnings-related pensions reduced could meet resistance from the higher paid. This risk would probably be less if overall contribution rates were contained and if pensioners continued to be seen as a deserving group.

- equivalent cash benefits could be considered as an alternative to the existing age allowances which provide higher personal tax allowances for tax payers aged 65 or over, subject to an income limit. This would be advantageous for low income pensioners.

- means-testing procedures could be simplified and improved. For example, housing-related needs now met by supplementary benefit (eg heating additions, water rates) could be transferred to Housing Benefit which is generally regarded as less stigmatising than supplementary benefit and probably achieves a higher rate of take-up (among pensioners).

- the National Insurance system could be altered to shift the balance in favour of the low paid by reducing the rate of National Insuance contribution by eg increasing the Treasury supplement to the National Insurance Fund. This shift would enable the low paid to save more, if they so wished, for their retirement. There could also be a beneficial effect on the incentive for the unemployed to take on low paid work which might outweigh other work disincentive effects arising from higher general taxation.

Retirement Age

39. Ministers will have to judge the social value of earlier retirement but in so far as it is seen as a way of relieving unemployment, special reversible measures are preferable to a reduction in the national retirement age. Given the cost of the latter and worries about the possible burden of present pension commitments, the Government's first response to the Social Services Committee report should be to welcome its conclusion that a retirement age for men of 60 is positively undesirable.

40. Unfortunately, the practical effect of a number of the Committee's proposals would be to provide a financial inducement for people to retire early. In particular, the Committee recommends: more generous pensions than would be justified actuarially for people opting to retire before a common retirement age of 63; a minimum pension income guarantee which would in effect mean retirement at 60 on approximately full pension for the lowest paid; and restoration of full pension for survivors whose deceased spouses retired early on an abated pension. Moreover, there are three additional risks of increased expenditure:

- there could well be pressures to reduce the common pension age below 63 once this was established or else to reduce men's pension age but not increase women's;

- a facility to retire earlier than 63 on reduced pensions from age 60 could, as in other countries eg France, result in pressures to pay full instead of reduced pensions at that age. After allowing for savings on unemployment-related benefits, the DHSS estimate that a common retirement age of 60 could cost the state £2½ bn a year at current levels of pensions, rising considerably as the new state scheme matures, and occupational pension contributions might have to rise, according to the Government Actuary, by a third;

- a lower retirement age is likely to lead to pressure to extend age allowances to those below age 65, with tax loss implications.

41. Partly as a consequence of these pressures, and partly because the Committee did not cost its concessions to those retiring on abated pensions, the proposals could turn out very considerably more expensive than the Committee's own estimates (para 8 above) which may, in any case, underestimate the long run costs as the new state scheme matures. If Ministers accept the view that they should avoid new commitments which may not have top priority, then they should be chary of endorsing the Committee's approach, even in principle.

42. One way to obtain the benefits of a more flexible pension age, while limiting the attendant costs and risks of the Committee's scheme, would be to:

(a) keep men's normal pension age at 65 and introduce an option to retire from 60 on a properly abated pension, retaining the current option to retire between 65 and 70 on an augmented pension; and, at the same time;

(b) progressively increase women's normal pension age to 65 and increase their retirement age band from 60-65 to 60-70. This would be a slow process, given the inevitable opposition and the lack of a compensating reduction in men's pension age. Depending on what changes were made to the state scheme, the rising schedule of entitlements now envisaged might provide headroom over the next 15 years to raise women's pension age, given adequate safeguards for those already near retirement;

(c) either, accept that the early retirement option would have the unfortunate consequence of increasing dependency on supplementary benefit in old age or limit the option to people whose total income would exceed a specified minimum sufficient to keep them off supplementary benefit in their declining years. The latter option would be administratively cumbersome and is likely to be criticized as unfair.

The benefits of such a package, in terms of equality, greater freedom of choice and expenditure savings from a higher pension age for women, might, in the event, not justify the disadvantages and political costs. A facility to retire earlier than at a common age of 65 could pose particular difficulties until pensioners are generally better provided for, eg in the next century.

Occupational Pensions and Personal Retirement Saving

43. It was noted above (para 35 et seq) that Ministers might wish to move towards the more limited but important role for the state of preventing poverty in old age, thereby placing more of the responsibility for "income replacement" on the individual. If this is accepted, consistency demands that parallel measures be taken to improve the opportunities for everyone for personal retirement saving and to rectify the deficiencies of occupational pension schemes.

44. We believe the principal weaknesses of the present arrangements for providing retirement incomes relate to:

- the general ignorance of individuals of their pension rights and pension costs. This ignorance is partly the result of paternalism, not only of the state but also of employers. Even those with the best of intentions typically compel employees to join the company's occupational pension scheme;

- the tax arrangements for retirement saving which, for approved funds, may be too generous and which distort financial markets by providing unequal treatment to different channels of saving;

- the position of employees with typically mobile patterns of employment in private sector occupational pension schemes (see para 15(a) above);

- the failure to provide reasonable inflation-proofing of pensions in payment in the private sector;

- the uncertain status of pension promises in occupational schemes (which raises questions about employer obligations to meet employee expectations).

45. The CPRS believes there is a number of general remedies which are desirable:

- better basic schooling to prepare people for life's financial responsibilities;

- the issue by government of indexed financial securities of adequate amount and with a sufficient spread of maturities to encourage intermediaries to offer inflation-proof retirement savings plans;

- the removal of economically-distorting fiscal arrangements which effectively mean that the range of tax-efficient savings plans, open to those outside the occupational pension sector, is limited to those offered by insurance companies. Equal tax treatment of different channels of saving (including saving through banks and building societies - but possibly less generous than that now offered pension funds) would reduce distortions, widen choice and stimulate competition between, and thus innovation by, the various intermediaries. Such reforms could be addressed to long term saving alone or, more radically, to all saving. It might also be desirable to consider tax arrangements which could stimulate voluntary individual saving by those on low and moderate incomes who benefit less than others from a straightforward deduction of pension contributions from their personal tax base. Reforms in this area will be difficult, if only because of the vested interests of pension funds. They therefore require a politically as well as technically imaginative approach.

46. For the occupational pension sector, reform has to recognise the constraint on resources. Mention has already been made of the fact that an extension of "Rolls Royce" public sector pensions to the private sector could be prohibitively expensive. In today's climate, the preferable strategy would be for private sector schemes to aim at a better quality of provision - especially in protecting pensions in payment against inflation and in providing for early leavers - and to accommodate this by reducing the size of the pension that schemes promise to pay in relation to members' salary. Most occupational schemes calculate a member's pension as a fraction (eg a 60th - the "accrual rate") of his final salary multiplied by the number of years of service attributed to the member. The size of the promised pension could therefore be reduced by lowering the rate of accrual of the pension (eg from a 60th to an 80th, the latter rate being the minimum now required in order for a scheme, which has also to satisfy other requirements, to contract-out). A less ambitious target for the size of occupational pensions promised by schemes would not only facilitate the introduction of desirable improvements in pension benefits, it would also improve the chances of actual delivery of the promised benefits. Access to schemes for additional voluntary contributions should be made available for all members of occupational schemes who wish to purchase added pension benefits and thus a higher level of income replacement in retirement.

47. The main difficulty which faces such a strategy is that, in all likelihood, private sector scheme members, particularly those now cross-subsidised by others, will not agree voluntarily to lower promised benefits, even though for many members the benefits are illusory or purchased at comparatively high cost. There is no easy solution to this problem. One way would be to impose a statutory duty on schemes to make desirable improvements (eg for early leavers), leaving schemes to finance this as best they can. But overt intervention of this sort may backfire by encouraging scheme members to expect, and therefore demand, quality improvements without compensating reductions in the level of pension promises.

48. An alternative route, less exposed to this risk, would be to create a climate in which decisions - either to pay extra for "Rolls Royce" pensions or to balance desired improvements with lower promised pension benefits - were taken in a decentralised way, through collective bargaining between employers and members of individual schemes. If this is to work, the main requirement will be to strengthen the bargaining position of those members - especially early leavers - who stand to lose from current arrangements. The reality remains that, if employers and members are not willing to increase their overall pension contributions, the raising of benefits for losers ultimately means less benefits for high flyers and stayers who are subsidized by final salary occupational schemes.

49. While any attempt to rectify the deficiencies of occupational pension schemes is almost certain to be controversial and meet resistance, we suggest in the following five paragraphs an approach to reform.

<u>Public v Private Sector Provision</u>

50. To encourage adjustment in the private sector, perceived and actual disparities between the public and private sectors should be reduced by ensuring that public sector schemes are contributory and integrated with the basic state pension (see para 12 above). More radically, accrual rates in public sector schemes could be reduced, in cases where it was feasible to reflect this in lower rates of contribution. Solvency guarantees, especially in the nationalised industries, could be removed.

Visibility

51. The attraction and growth of final salary occupational schemes is linked to the perception of employees that a benefit defined in these terms provides them with economic security - even when there is no legal backing to the pension promise, the employer is seen to have a moral obligation to ensure that the promises of a certain level of income replacement are kept. However, the willingness of the employer to take on these moral obligations explains, at least in part, why he is unwilling to guarantee inflation-proofing for pensioners and, least of all, for early leavers. In this way, the cost of the moral obligation is spread, but unequally and with potentially adverse economic consequences (eg on employee mobility).

52. In so far as they are undesirable, it is likely that these features persist because of the vested interests of employers, stayers and others, because of ignorance - the nature of the gamble that faces all scheme members, stayers (as pensioners) as well as potential early leavers is not explained - and because of an absence of choice (see below). As a first step, reform must therefore aim to increase the visibility of pension arrangements. Fuller disclosure should aim to create an informed scheme membership with no illusions about final salary promises. (This could have the added advantage of developing a wider constituency and interest by members in the investment performance of pensions funds, thereby limiting the risk of political direction of funds.) Further improvements in visibility will come if employees share more equally amongst themselves and with the employer the obligation for the delivery and guarantee of benefits. In particular, appropriate public sector schemes could lead in the development of a fixed relationship between contributions by employer and employee, thus ensuring that both parties share formally in the success or deficiencies of the pension fund. Relieved of the full weight of his moral obligation, the employer should be obliged to treat better those whom schemes now penalise. For example, the benefits of early leavers and of those already retired should be inflation-proofed as securely as the accruing rights of those still contributing.

Competition and Choice

53. The development of alternatives to final salary schemes provides an important and final string to the bow of reform. The main contender is the "defined contribution plan", so named because benefits are defined by the record of contribution by employer, if any, and by the employee and are, in addition, dependent on the return on the fund. These benefits are vested in the individual who therefore has a portable pension. The employer is unlikely in such schemes to guarantee any particular level of benefit. The performance of the fund therefore takes on a key role. Traditional money purchase arrangements are the most common form of defined contribution plan and should be able to evolve into sophisticated versions which, although not offering a cast iron guarantee, vary the rate of contribution in order to produce on average a certain level of income replacement.

54. The strengths of defined contribution plans in terms of visibility, vesting and portability make efforts to encourage their development worthwhile. As a first step, the rules for contracting-out of occupational schemes could be widened to embrace sophisticated, high quality money purchase schemes. Together with the measures to facilitate indexation and equal tax treatment of savings channels, this could stimulate development of sophisticated money purchase schemes offered by companies alongside the existing structure of final salary schemes. However, the major impact on final salary schemes, and thus pressure for reform, would come if employees of the same company could choose between different types of scheme offered by their employer - between a defined benefit final salary scheme and a defined contribution plan - and/or between the employer's scheme(s) and defined contribution plans offered by other intermediaries. This radical option could eventually have a significant impact on the occupational pension sector and arguably make it not only healthier and more equitable, but also more adaptive to the needs of a rapidly changing and evolving economy (cf objectives in para 17(e) and (f)). The advantages and practical difficulties of this route to better pensions are discussed in detail in the companion CPRS paper: "Pensions and Individual Choice.

FUTURE WORK

55. This note has outlined various possible objectives and constraints facing pensions policy and highlighted a number of broad issues. In approaching the subject, Ministers should first review their objectives (para 17). In particular, there is a need to reconsider the role of the state - do Ministers agree that its prime role should be to prevent poverty in old age, by a combination of selective (means-tested) benefits and the universal National Insurance pension, rather than to seek to guarantee a minimum level of "income replacement"? If poverty prevention is the main goal, the question of the balance of selectivity v universalism arises (para 26). Some of the possible options for change were noted in paras 36-38. And if the state is to play less of a direct role in "income replacement", there is a greater need to consider how opportunities can be widened for inflation-proof, tax-efficient retirement saving for those in occupational schemes and those outside. Reform of non-state pensions needs also to fit in with Ministers' economic aims. Possible options for reform were outlined in para 43 et seq.

56. Ministers should then consider the nature of the constraints they face (paras 19-22). Given the risk of an excessive burden of pensions in the long term, Ministers should examine ways of limiting, if not reducing, both state and non-state pension entitlements in ways which are consistent with their objectives. We have outlined how cutbacks in state earnings-related entitlements could be made more politically attractive within a rounded package of measures. The problems facing policy on retirement age were discussed in paras 39-42. We have not, however, suggested how changes in the tax treatment of savings might be approached - either with a view to cutting back or with more general reforms in mind. Possible modest tax changes were recommended in earlier reports by a Treasury-led group on Tax and Savings. In a second term of office, Ministers could take a fresh look at the subject with a view to making more radical changes.

57. Some of the extra work which will be required to follow up individual issues will evolve naturally from work which officials already have in hand. Other key topics, not covered or only incompletely covered, by existing work are:

- the costs and implications of various options to prevent poverty in old age while reducing the earnings-related element of the state pension scheme;

- measures to reduce disparities in pension provision as between public and private sector occupational schemes;

- reform of the tax treatment of retirement and other savings and of pensioners' incomes.

Ministers need to consider whether they wish to commission further study of relevant issues.

CONFIDENTIAL

45

DEPARTMENT OF HEALTH & SOCIAL SECURITY

Alexander Fleming House, Elephant & Castle, London SE1 6BY

Telephone 01-407 5522 ext 6905

G A Hart Esq
Cabinet Office
Central Policy Review Staff
70 Whitehall
London SW1A 2AS

April 1983

CABINET OFFICE
Mcl 45
27 APR 1983
INSTRUCTIONS
5/33

Dear Graham,

CPRS REPORT ON PENSIONS

destroyed CAH 28/4

As requested, I return the three copies of the earlier draft which you sent us. I confirm that I have recovered and destroyed the only other two copies which we had to make, with Ministers' agreement. I also confirm that, as I suggested on the telephone, I am recovering the copies of the very few and limited circulation minutes which I wrote in preparing my comments on 22 March and 12 April.

Yours ever,

Michael

M J A PARTRIDGE

CONFIDENTIAL

CABINET OFFICE

Central Policy Review Staff

70 Whitehall, London SW1A 2AS Telephone 01-233 5029

Hd.0167

18 April 1983

G W Monger Esq
HM Treasury
Parliament Street
SW1

Dear George

CPRS PAPERS ON PENSIONS

I wrote to you on 17 March enclosing copies of the draft documents 'Pensions Issues and Policy' and 'Pensions and Individual Choice'. We have corresponded since about your comments on them.

I would be grateful if you would now arrange for the return to me of the drafts that were sent to your Department, which for convenience I list below -

Copies	No 13	-	yourself
	No 14	-	Mr Monck
	No 15	-	Mr Moore
	No 16	-	Mr St Clair

Yours ever

Graham

G A HART

CONFIDENTIAL

CABINET OFFICE

Central Policy Review Staff

70 Whitehall, London SW1A 2AS Telephone 01-233 5029

Hd.0166

18 April 1983

T J Painter Esq
Inland Revenue
Somerset House
London WC2R 1LB

Dear Painter

CPRS PAPERS ON PENSIONS

I wrote to you on 17 March enclosing copies of the draft documents 'Pensions Issues and Policy' and 'Pensions and Individual Choice', and we have now received helpful comments in John Isaac's letter of 31 March.

I would be grateful if you would now arrange for the return to me of the drafts that were sent to your Department, which for convenience I list below -

Copies	No 7	-	Mr Isaac
	No 8	-	Mr O'Leary
	No 9	-	yourself
	No 22	-	Mr H B Thompson (SFO)

Yours sincerely

Graham Hart

G A HART

CONFIDENTIAL

CONFIDENTIAL

CABINET OFFICE
Central Policy Review Staff
70 Whitehall, London SW1A 2AS Telephone 01-233 5029

Hd. 0165

18 April 1983

E A Johnston Esq CB
Government Actuary's Department
22 Kingsway
London WC2B 6LE

Dear Johnston

CPRS PAPERS ON PENSIONS

I wrote to you on 17 March enclosing copies of the draft documents 'Pensions Issues and Policy' and 'Pensions and Individual Choice'. We have since discussed them and we are grateful to you for your considerable help.

I would be grateful if you would now arrange for the return to me of the drafts that were sent to you.

Yours sincerely
Graham Hart

G A HART

CONFIDENTIAL

Mr Hart
11(A)

CABINET OFFICE
Central Policy Review Staff
70 Whitehall, London SW1A 2AS Telephone 01-233 5029

Hd.0164

18 April 1983

M J A Partridge Esq
DHSS
Alexander Fleming House
Elephant & Castle
London SE1 6BY

Dear Michael

CPRS PAPERS ON PENSIONS

I wrote to you on 17 March enclosing copies of the draft documents 'Pensions Issues and Policy' and 'Pensions and Individual Choice', and we have since discussed them.

I would be grateful if you would now arrange for the return to me of the drafts that were sent to the Department, which for convenience I list below -

Copies	No 10	-	yourself
	No 11	-	Sir Geoffrey Otton
	No 12	-	Mr Ward

Yours ever

Graham

G A HART

CONFIDENTIAL

11 (A)

copy sent to
Mr O'Leary

CABINET OFFICE

Central Policy Review Staff

70 Whitehall, London SW1A 2AS Telephone 01-233 5029

Hd.0155

24 March 1983

H B Thompson Esq
Controller, Inland Revenue,
Superannuation Funds Office
Lynwood Road
Thames Ditton
Surrey KT7 0DP

Dear Mr Thompson

CPRS REPORTS ON PENSIONS

As arranged with Peter O'Leary I enclose copies of two draft CPRS reports 'Pension Issues and Policy' and 'Pensions and Individual Choice'. In accordance with the procedure agreed between Mr Sparrow here and Sir Lawrence Airey, these documents are not to be copied and are to be returned to me when the consultation process is complete. They should not be shown to anybody else except on a strict 'need to know' basis.

Yours sincerely

pp G A HART

Mr Cleaver

Note
Mr Hart's copies (22)
sent to Mr Thompson,
(to be returned to him)

CONFIDENTIAL

CABINET OFFICE
Central Policy Review Staff
70 Whitehall, London SW1A 2AS Telephone 01-233 5029

Hd.0149

17 March 1983

T J Painter Esq
Inland Revenue
Somerset House
London WC2R 1LB

Dear Painter,

CPRS WORK ON PENSIONS

We are now approaching the time when we shall be ready to submit to Ministers the first fruits of our recent work in the field of pensions. This will consist of two documents. One - 'Pensions Issues and Policy' - attempts to survey briefly some of the principal issues that will be or should be coming to Ministers soon for decision and to set them within a policy framework. The second, - 'Pensions and Individual Choice' is a more detailed examination of the idea of the portable occupational pension which could play an important part in meeting Ministers' objectives.

2. I enclose a copy of the latest versions of the two draft papers - on which we ourselves will continue working - and we would be very grateful for any comments that your Department might care to make on them. It would be helpful if these could be in writing by 25 March. If you think a discussion would also be useful we should be happy to organise one.

3. I am sending a copy of this letter and enclosures to John Isaac and Peter O'Leary; this is on the basis set out in John Sparrow's letter of 10 March to Sir Lawrence Airey.

4. I am writing in similar terms to Edward Johnston (GAD), George Monger (Treasury) and Michael Partridge (DHSS).

Yours sincerely
Graham Hart

G A HART

CABINET OFFICE
Central Policy Review Staff
70 Whitehall, London SW1A 2AS Telephone 01-233 5029

Hd.0148 17 March 1983

G W Monger Esq
HM Treasury
Parliament Street
SW1

Dear George

CPRS WORK ON PENSIONS

We are now approaching the time when we shall be ready to submit to Ministers the first fruits of our recent work in the field of pensions. This will consist of two documents. One - 'Pensions Issues and Policy' - attempts to survey briefly some of the principal issues that will be or should be coming to Ministers soon for decision and to set them within a policy framework. The second, - 'Pensions and Individual Choice' is a more detailed examination of the idea of the portable occupational pension which could play an important part in meeting Ministers' objectives.

2. I enclose a copy of the latest versions of the two draft papers - on which we ourselves will continue working - and we should be very grateful for any comments that your Department might care to make on them. It would be helpful if these could be in writing by 25 March. If you think a discussion would also be useful we should be happy to organise one.

3. I am sending a copy of this letter and enclosures to Nick Monck, David Moore and Bill St Clair; this is on the basis set out in John Sparrow's letter of 10 March to Sir Douglas Wass.

4. I am writing in similar terms to Michael Partridge (DHSS), Edward Johnston (GAD), and Terry Painter (Inland Revenue).

Yours

Graham

G A HART

CONFIDENTIAL

CABINET OFFICE
Central Policy Review Staff
70 Whitehall, London SWIA 2AS Telephone 01-233 5029

Hd.0150

17 March 1983

E A Johnston Esq CB
Government Actuary's Department
22 Kingsway
London WC2B 6LE

Dear Johnston,

CPRS WORK ON PENSIONS

We are now approaching the time when we shall be ready to submit to Ministers the first fruits of our recent work in the field of pensions. This will consist of two documents. One - 'Pensions Issues and Policy' - attempts to survey briefly some of the principal issues that will be or should be coming to Ministers soon for decision and to set them within a policy framework. The second, - 'Pensions and Individual Choice' is a more detailed examination of the idea of the portable occupational pension which could play an important part in meeting Ministers' objectives.

2. I enclose a copy of the latest versions of the two draft papers - on which we ourselves will continue working - and we would be very grateful for any comments that your Department might care to make on them. It would be helpful if these could be in writing by 25 March. If you think a discussion would also be useful we should be happy to organise one.

3. We spoke about the need to safeguard the confidentiality of these papers. The basis on which we are operating is that recipients of the papers are responsible for safeguarding them; that the papers may not be copied; that they may be shown to anyone in your Department on a strict need-to-know basis; and that when the consultation process is completed the papers should be returned to us.

4. I am writing in similar terms to Michael Partridge (DHSS), George Monger (Treasury) and Terry Painter (Inland Revenue).

Yours sincerely

Graham Hart

G A HART

CONFIDENTIAL

Mr Hart

11(A)

CABINET OFFICE
Central Policy Review Staff

Hd.0147

17 March 1983

70 Whitehall, London SW1A 2AS Telephone 01-233 5029

M J A Partridge Esq.,
DHSS
Alexander Fleming House
Elephant & Castle
London SE1 6BY

Dear Michael,

CPRS WORK ON PENSIONS

We are now approaching the time when we shall be ready to submit to Ministers the first fruits of our recent work in the field of pensions. This will consist of two documents. One - 'Pensions Issues and Policy' - attempts to survey briefly some of the principal issues that will be or should be coming to Ministers soon for decision and to set them within a policy framework. The second, - 'Pensions and Individual Choice' is a more detailed examination of the idea of the portable occupational pension which could play an important part in meeting Ministers' objectives.

2. I enclose a copy of the latest versions of the two draft papers - on which we ourselves will continue working - and we would be very grateful for any comments that your Department might care to make on them. It would be helpful if these could be in writing by 25 March. If you think a discussion would also be useful we should be happy to organise one.

3. I am sending a copy of this letter and enclosures to Sir Geoffrey Otton and Joe Ward; this is on the basis set out in John Sparrow's letter of 10 March to Sir Kenneth Stowe.

4. I am writing in similar terms to Edward Johnston (GAD), George Monger (Treasury) and Terry Painter (Inland Revenue).

Yours
Graham

G A HART

CONFIDENTIAL

CONFIDENTIAL

11(A)

H M Treasury

Parliament Street London SW1P 3AG

Switchboard 01-233 3000
Direct Dialling 01-233 3620

Sir Douglas Wass GCB
Permanent Secretary

CABINET OFFICE
Q 3319
16 MAR 1983
FILING INSTRUCTIONS
FILE No.

Mr John Sparrow
CPRS
Cabinet Office
Whitehall
LONDON
SW1

16 March 1983

1 Mr Caines
2 Mr Sparrow
C. Mr Hart
C. Mr Beauman
C 1 Miss Mackay
2 Mr Martin
3 Mr Smee.

Dear John.

CPRS REPORT ON PENSIONS

Thank you for your letter of 10 March.

I am quite content with the procedure you propose. In the Treasury, however, there are at least four Groups with an interest. Since copying of papers will not be permitted, I hope I may therefore make four nominations in our case. The nominations are of George Monger, who will co-ordinate the comments, Nick Monck, David Moore and Bill St Clair.

I am sending a copy of this letter to Robert Armstrong.

Yours ever,

Douglas

DOUGLAS WASS

CONFIDENTIAL

DEPARTMENT OF HEALTH & SOCIAL SECURITY

Alexander Fleming House, Elephant & Castle, London SE1 6BY

Telephone 01-407 5522 ext 6981

From the Permanent Secretary

Sir Kenneth Stowe KCB CVO

1. Mr Cassie
2. Mr Sparrow

c 1. ~~Mr Hewitt~~
2. ~~Mr Mountfield~~
3. ~~Mr Hawkins~~

c. Mr Reason

Your ref: Qa 06293

John Sparrow Esq
Cabinet Office
80 Whitehall
London
SW1A 2AS

CABINET OFFICE
Qa 3310
15 MAR 1983
FILING INSTRUCTIONS
FILE No.

15 March 1983

Dear John.

CPRS REPORT ON PENSIONS

Thank you for your letter of 10 March. We do, of course, understand the need to ensure that this document is properly safeguarded. The "lead" contact here would be Michael Partridge (Room D603 in this building) and I should be grateful if copies could also go to Sir Geoffrey Otton (Room D601) and to Joe Ward, (the Under Secretary responsible who is in Room 913, State House, High Holborn, WC1).

I am copying this to Douglas Wass, Lawrence Airey and Robert Armstrong.

Yours ever.

Ken.

CONFIDNETIAL

CONFIDENTIAL

11(A)

THE BOARD ROOM

INLAND REVENUE, SOMERSET HOUSE LONDON WC2R 1LB

TELEPHONE 01-438 6494/6615

FROM THE CHAIRMAN

CABINET OFFICE
Q3 3295
14 MAR 1983
FILING INSTRUCTIONS
FILE No.

14 March 1983

John Sparrow Esq
Cabinet Office
Central Policy Review Staff
70 Whitehall
London SW1

1. Mr Carnies
2. Mr Sparrow

c1. Mr Hunt
2. Mr Beaumont
3. Mr Martin
4. Miss Mackay

Dear John

CPRS REPORT ON PENSIONS

Thank you for your letter of 10 March.

I am content with the arrangements you propose and will nominate the responsible Deputy Chairman, John Isaac; the Under-Secretary directly concerned, Peter O'Leary; and the Under-Secretary Central Division, Terry Painter, as recipients of the draft in this Department. They will certainly need to show the draft to one or two others (including myself) but this will be on a strict need to know basis. Terry Painter will be responsible for co-ordinating our comments.

Copies to the recipients of your letter.

Yours ever

Lawrence

Lawrence Airey

Pl. file

D

CABINET OFFICE

Central Policy Review Staff

70 Whitehall, London SW1A 2AS Telephone 01-233 7765

Qa 06293

From: John Sparrow

CONFIDENTIAL

10 March 1983

Sir Kenneth Stowe KCB CVO
Department of Health & Social Security
Alexander Fleming House
S E 1

Dear Ken,

CPRS Report on Pensions

As you will know we were asked by the Prime Minister last Autumn to undertake a study on pensions.

We are now approaching the end of our work on this and would like to follow our usual practice of giving the principal interested Departments an opportunity of looking over our draft report before we complete it for submission to Ministers. But I need to find a way of doing this which takes account of current concerns about proper safeguarding of sensitive documents issuing from the Cabinet Office. I would like to suggest the following procedure:

> You nominate one or more (perhaps three as a maximum) officials in your Department who would each receive and be responsible for safeguarding a copy of our draft. No copying would be permitted. It would be up to the nominated officials to decide whether they needed to show the report to anybody else but they should adopt a strict need-to-know test. One nominated official should be responsible for co-ordinating any comments to us. After the consultation process has been completed all of the copies would be returned to us.

If you agree with this I should be grateful if you could let me know the name or names of those to whom we should entrust a copy of our draft and which of them would be the 'lead' contact for us.

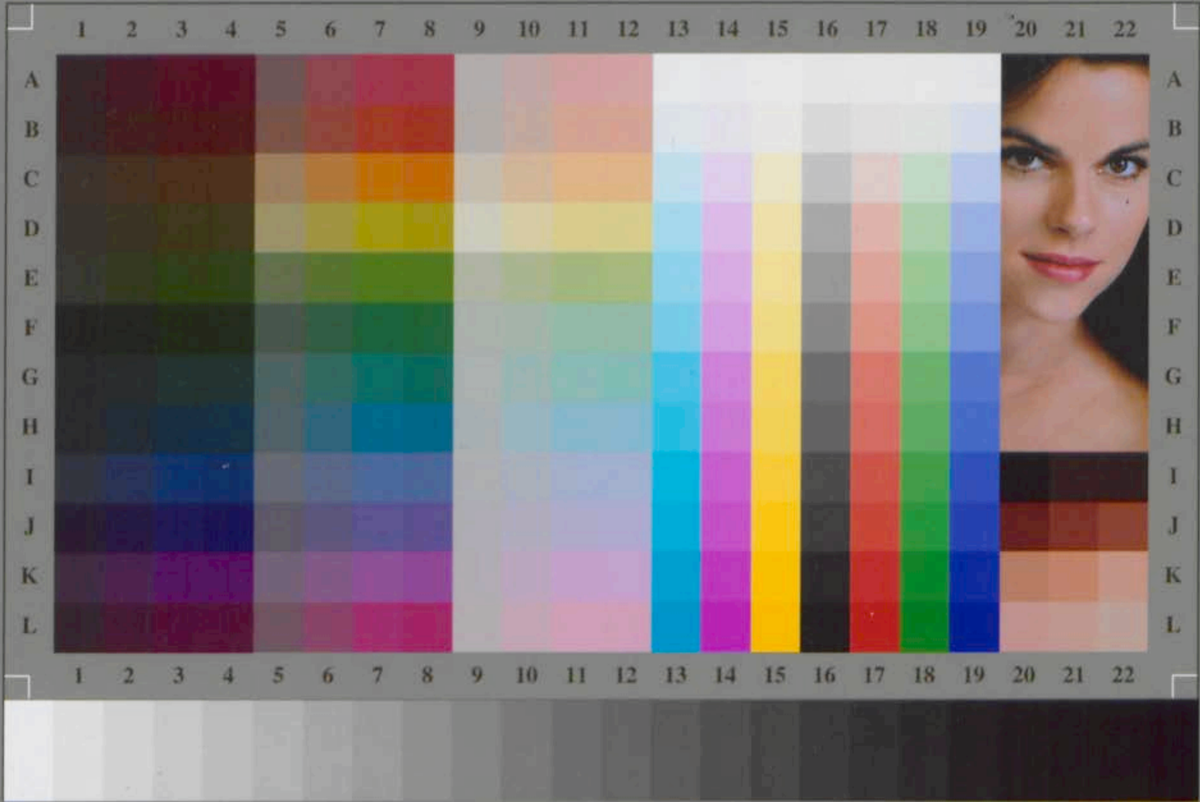
I am writing in similar terms to Douglas Wass and Lawrence Airey, and am copying to Robert Armstrong for information.

Yours sincerely,

John

KODAK Q-60 Color Input Target

C M Y



IT8.7/2-1993
2007:03

FTP://FTP.KODAK.COM/GASTDS/Q60DATA

Q-60R2 Target for
KODAK
Professional Papers