



SECRET

~~CCDW~~
39

PRIME MINISTER

MISC 111: PROVISION FOR RETIREMENT

We agreed at the second meeting of MISC 111 on 13 February that a compulsory occupational pension scheme should be introduced after the State earnings-related pension scheme (SERPS) is abolished in 1987. My paper discussed at that meeting (MISC 111(85)5) set out the framework of such a scheme. Colleagues may now like to know more about how I see it operating.

MISC 111 favoured early introduction of the compulsory scheme - if possible in 1987. I am convinced that we should aim for this. It will mean that there is no gap between SERPS and its successor and that the new scheme will be fully operational before an election. Pension rights will start building up for everyone. By contrast, a transitional period would mean a gap between SERPS and the new scheme for those most likely to need additional pensions (and who would otherwise need means-tested help. Even with inducements, employers who have hitherto resisted setting up a pension scheme are likely to leave it until the last minute.

If the response to the Green Paper suggests that a full start in 1987 is unrealistic, we might go for a short phasing in period of no more than three years. I would then regard it as essential to give employers some form of national insurance contribution concession during that period. That would give them more time to get their schemes set up and encourage them to do so as soon as possible. We agreed that the form of the scheme should be a "money purchase" one with a minimum percentage of an employee's earnings required as a pension contribution and the employer meeting at least half of this. I envisage that minimum as being around 5%

SECRET

or 4% of earnings, to keep down burdens on employers. Schemes would have to provide as a minimum a pension (indexed after award by the lesser of 5% and the RPI) and survivors' benefits.

The other major features of the occupational scheme are

- coverage should be as complete as possible. I propose to exclude only new employees (say for the first 6 months) and those on very low earnings, perhaps below the lower earnings limit for national insurance contributions, to avoid the danger of supplementary benefit dependence.

- everyone would be able to choose a personal pension instead of joining an employer's scheme. In that case, the same minimum contributions would be required as for the compulsory occupational scheme, at least half being met by the employer.

- self-employed people will be included in the compulsory scheme. Again, we shall need some exemption for those with very low profits, perhaps tied to the small earnings exception for Class 2 national insurance contributions.

- schemes basing pensions on a promised level of benefit (e.g. related to final salary) would be able to meet the compulsory requirements on the basis of a contribution test. Schemes at present contracted-out would qualify automatically.

- protection of pension investments is also a subject on which I shall invite views in the Green Paper. Norman Tebbit's proposed framework for investor

protection is a very substantial step forward. But we shall need additional controls and safeguards, particularly to cover self-administered pension schemes and to limit administrative charges. This is a matter which I shall discuss further with Norman Tebbit. The annexes to this minute show the effect of a compulsory scheme on employers' and employees' wage costs and the pensions which people can expect under the scheme, compared with what they would have got from SERPS.

I shall be discussing separately with Treasury Ministers the implications of the compulsory scheme for the indexation of public sector pensions. I am also giving further thought, as the Group wanted, about the penalties for non-compliance and I shall consult Leon Brittan about these.

The result of these proposals will be that almost everyone who has been in work will have an occupational pension; and at any one time over 80% of the workforce will be in schemes, compared with only 50% now.

I am copying this minute to the members of MISC 111, Keith Joseph, Patrick Jenkin and Norman Tebbit, and to Sir Robert Armstrong.

29 March 1985

SAJ

for NF

(Approved by the Secretary of State
and signed in his absence)

29

OVER

COMMENTS

THE EFFECT OF A COMPULSORY OCCUPATIONAL SCHEME ON EMPLOYERS' AND EMPLOYEES' COSTS

A. WITH A MINIMUM CONTRIBUTION OF 4% OF EARNINGS (2% A SIDE)

1. EMPLOYERS

Weekly earnings £	<u>Contracted-in</u>		<u>Contracted-out (NIC only)</u>	
	1985/86 (NIC)	After change (NIC + pension cont)	1985/86	After change
50	2.50	2.50	1.91	1.50
70	4.90	4.90	3.49	3.50
100	9.00	9.00	6.36	7.00
120	10.80	10.80	7.34	8.40
150	15.68	15.75	10.98	12.75
180	18.81	18.90	12.89	15.30
200	20.90	21.00	14.16	17.00
265	27.69	27.83	18.28	22.53
500	52.25	52.50	42.84	42.50

2. EMPLOYEES

50	2.50	2.50	2.19	1.50
70	4.90	4.90	4.16	3.50
100	9.00	9.00	7.62	7.00
120	10.80	10.80	8.99	8.40
150	13.50	15.00	11.04	12.00
180	16.20	18.00	13.10	14.40
200	18.00	20.00	14.47	16.00
265	23.85	26.50	18.92	21.20
(UEL)				

B. WITH A MINIMUM CONTRIBUTION OF 5% OF EARNINGS (2½% A SIDE)

3. EMPLOYERS

Weekly earnings £	<u>Contracted-in</u>		<u>Contracted-out (NIC only)</u>	
	1985/86 (NIC)	After change (NIC + pension cont)	1985/86	After change
50	2.50	2.75	1.91	1.50
70	4.90	5.25	3.49	3.50
100	9.00	9.50	6.36	7.00
120	10.80	11.40	7.34	8.40
150	15.68	17.25	10.98	12.75
180	18.81	19.80	12.89	15.30
200	20.90	22.00	14.16	17.00
265	27.69	29.16	18.28	22.53
500	52.25	55.00	42.84	42.50

4. EMPLOYEES

50	2.50	2.68	2.19	1.50
70	4.90	5.15	4.16	3.50
100	9.00	9.35	7.62	7.00
120	10.80	11.22	8.99	8.40
150	13.50	15.53	11.04	12.00
180	16.20	18.63	13.10	14.40
200	18.00	20.70	14.47	16.00
265	23.85	27.43	18.92	21.20
(UEL)				

Notes

1. For contracted-in employees the effects of change are shown net of 30% tax relief on their pension contributions. This means an actual contribution of 0.7% of earnings for each 1% stipulated as a minimum.

2. 1985/86 figures embody the changes announced in the Budget and due to come in in October.

3. It is assumed that the NI contribution reliefs for low paid employees on the lines announced in the Budget continue after the change. The combined NIC rate is assumed to be 16.5% (the latest GAD estimate), split 8.5% - 8% between employer and employee. Special rates for the low paid are assumed to be successively 3%, 5% and 7% a side.

4. 1985/86 figures are for NIC only. "After change" ones are NIC only for the contracted-out and NIC + 2% pension contribution for others. This is because the only extra burdens on contracted-out people will be from higher NIC rates: they will already be in occupational schemes that will qualify under the new arrangements.

5. NIC rates for people now contracted-out will rise because of the abolition of SERPS (it is from the earnings-related part of the State scheme that they can now contract-out): and the end of lower contracting-out rates will bring full rates down. For contracted-out employers with employees on high earnings, this will mitigate the effect of abolishing the UEL for employers. From October they will pay full-rate contributions on earnings up to the LEL and above the UEL; the tables show that for earnings of about £500 upwards, the savings from the full rate going down will be greater than the costs of the lower contracted-out rate ceasing to exist.

SERPS AND COMPULSORY OCCUPATIONAL SCHEME: COMPARATIVE BENEFITS FOR A MAN ON £100 PW EARNINGS AT 1984/85 LEVELS FROM 4% CONTRIBUTION

1 Age in 1987/88	2 Final earnings	3 Full SERPS	4 SERPS pension	5 Compulsory pension with rate of return over prices of 3½%	6 Total	7 2½%	8 Total
£ per week at 1984/85 prices							
25	177.40	29.30	3.60	29.10	32.70	23.40	27.10
35	154.30	25.50	6.00	17.30	23.30	14.80	20.80
45	134.10	22.10	7.10	8.60	15.70	8.10	15.20
55	116.60	17.30	8.70	3.30	11.90	3.30	11.90
As % of final earnings							
25		16.5	2.0	16.4	18.4	13.2	15.3
35		16.5	3.9	11.2	15.1	9.6	13.5
45		16.5	5.3	6.4	11.7	6.0	11.3
55		14.8	7.5	2.8	10.2	2.8	10.2

Notes

Column 3 shows the full earnings-related pension had SERPS continued;

Column 4 shows the actual (residual) pension from SERPS after its abolition;

Columns 5 and 7 show the private pension from contributions of 4%, and Columns 6 and 8 the total pension, by adding these to Column 4. Basic pension is excluded.

SERPS rights are assumed to be preserved on the same basis as GMPs (a separate submission is being prepared on this).

Final earnings are shown as higher than £100 because earnings grow faster than prices by 1½% per annum.

Private pension contributions earn a rate of return in excess of price inflation of 3½% in Column 5 and 2½% in Column 7. Men are assumed to contribute continuously to private pensions from 1987 onwards.

Private pensions are increased in line with prices once in payment up to 5% a year. A widow's pension equal to half the man's pension rights is also provided.

SECRET

SERPS AND COMPULSORY OCCUPATIONAL SCHEME: COMPARATIVE BENEFITS FOR A MAN ON £100 PW EARNINGS AT 1984/85 LEVELS FROM 5% CONTRIBUTION

1	2	3	4	5	6	7	8
Age in 1987/88	Final earnings	Full SERPS	SERPS pension	Compulsory pension with rate of return over prices of			
				3½%	Total	2½%	Total
£ per week at 1984/85 prices							
25	177.40	29.30	3.60	36.40	40.00	29.30	32.90
35	154.30	25.50	6.00	21.60	27.60	18.50	24.50
45	134.10	22.10	7.10	10.80	17.90	10.10	17.20
55	116.60	17.30	8.70	4.10	12.80	4.10	12.80
As % of final earnings							
25		16.5	2.0	20.5	22.5	16.5	18.5
35		16.5	3.9	14.0	17.9	12.0	15.9
45		16.5	5.3	8.0	13.3	7.5	12.8
55		14.8	7.5	3.5	11.0	3.5	11.0

Notes

Column 3 shows the full earnings-related pension had SERPS continued;

Column 4 shows the actual (residual) pension from SERPS after its abolition;

Columns 5 and 7 show the private pension from contributions of 5%, and Columns 6 and 8 the total pension, by adding these to Column 4. Basic pension is excluded.

SERPS rights are assumed to be preserved on the same basis as GMPs (a separate submission is being prepared on this).

Final earnings are shown as higher than £100 because earnings grow faster than prices by 1½% per annum.

Private pension contributions earn a rate of return in excess of price inflation of 3½% in Column 5 and 2½% in Column 7. Men are assumed to contribute continuously to private pension from 1987 onwards.

Private pensions are increased in line with prices once in payment up to 5% a year. A widow's pension equal to half the man's pension rights is also provided.

29 MAR 1985

10. 11. 12. 13. 14. 15.
9. 8. 7. 6. 5.

SECRET



DEPARTMENT OF HEALTH AND SOCIAL SECURITY
Alexander Fleming House, Elephant & Castle, London SE1 6BY
Telephone 01-407 5522

From the Secretary of State for Social Services

Mark Addison Esq
Private Secretary
10 Downing Street

29 March 1985

Dear Mark

MISC 111: PROVISION FOR RETIREMENT

I regret the attached was omitted from the minute from my Secretary of State to the Prime Minister sent round earlier today.

I am copying this letter to the Private Secretaries to members of MISC 111, Elizabeth Hodgkinson (Department of Education and Science), John Ballard (Department of the Environment), Callum McCarthy (Department of Trade and Industry) and to Richard Hatfield (Cabinet Office).

*Yours
Steve*

S A Godber
Private Secretary

SECRET