CABINET

NATIONAL SUPERANNUATION AND SOCIAL INSURANCE:
DRAFT WHITE PAPER

Note by the Secretary of State for Social Services

I invite the Cabinet to approve for publication the attached draft of a White Paper which embodies the proposals for an earnings-related pension scheme approved by the Cabinet at their meeting on 31st October (CC(68)45th Conclusions, Minute 5). I also seek the Cabinet's agreement to the preparation of legislation for introduction next Session.

R. H. S. C.

Department of Health and Social Security, S. E. 1.

13th December 1968
DEPARTMENT OF HEALTH AND SOCIAL SECURITY

National Superannuation and Social Insurance

PROPOSALS FOR EARNINGS-RELATED SOCIAL SECURITY

Presented to Parliament by the Secretary of State for Social Services by Command of Her Majesty January 1969

LONDON
HER MAJESTY'S STATIONERY OFFICE

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NATIONAL SUPERANNUATION AND SOCIAL INSURANCE
PROPOSALS FOR EARNINGS-RELATED SOCIAL SECURITY

INTRODUCTION

1. The Government are proposing the most fundamental changes in social security since the present national insurance scheme was introduced soon after the Second World War.

2. The present scheme is clearly inadequate. Nearly 30 per cent of all pensioners are dependent in some degree on supplementary benefit. The existing flat-rate scheme has failed, despite the effort made in 1961 to shore it up by introducing an element of graduated contribution and pension. And the extent of this failure will grow unless drastic steps are taken to reconstruct the whole system.

3. This White Paper sets out the Government's proposals for replacing the present national insurance scheme by a new scheme of national superannuation and social insurance, in which both contributions and benefits will be related to the earnings of the individual employee. The new earnings-related contributions will mostly be higher than the present-scheme contributions, especially for higher earners. But those who pay the new contributions will earn new and higher personal pensions and other benefits—personal in two particular senses. First, national superannuation pensions will be related to the individual's personal earnings record; the uniform flat-rate pension will go. Secondly, unlike pension rights under most private superannuation schemes, those under national superannuation will never be lost, however many times or for whatever reason the individual changes his job.

4. The new earnings-related pensions and other benefits will only be available to those who have paid the new contributions. Twenty years of new-scheme contributions will be required before the first pensions at the full new-scheme rates are paid to people reaching pension age then. These full rates will normally be adequate, even for those whose earnings have been relatively low, to live on without other means. Contributors who reach pension age during the twenty-year build-up period will earn pensions at intermediate rates. As more and more people draw the higher pensions which they will have earned by their new-scheme contributions, the proportion of pensioners needing supplementary benefit will gradually decline.

5. The new earnings-related pensions will not be available to those who are pensioners already. But existing pensioners will continue to share in the nation's rising living standards, through periodical increases in their pensions. The rate to be paid to present-scheme pensioners when the new scheme starts will be decided by the Government at the time.

6. The income of the new scheme will automatically rise as earnings rise. This buoyancy will help to make possible a new guarantee covering pensions and other benefits already in payment. The Government will be required by law to undertake a review every two years of the main rates of benefits.
in payment, both under the present scheme and under the new. The increases made will, as a minimum, compensate for any rise in prices during the two-year period. The amounts of increases beyond this will be decided by the Government of the day, in the light of the general situation on each occasion.

7. The Government have already introduced, in 1966, earnings-related short-term benefits for the first six months of sickness, unemployment and widowhood. Thus the most fundamental changes now proposed concern pensions and other long-term benefits. They are based upon broad principles formulated in "National Superannuation", published by the Labour Party in 1967. The Government's proposals are set out in this White Paper for public comment and debate, and to serve as a basis of consultation with both sides of industry and with organisations having a special interest in these matters. The Government plan to introduce legislation in the next session of Parliament, and to start the scheme as soon as possible afterwards. The target date is April 1972.

8. Part I of this White Paper explains why the present national insurance scheme has failed to provide adequate pensions (chapter 1). Part II sets out the Government's basic objectives under the new scheme (chapter 2); describes the scheme's main features (chapter 3); and gives the Government's reasons for rejecting two alternative approaches to pension reform—greater "selectivity", and reliance on occupational pension schemes (chapter 4). Part III deals with the State scheme's relations with occupational schemes (chapters 5 and 6), and Part IV with the financial and economic implications of the new scheme (chapter 7). Appendix 1 contains some further notes on particular aspects of the scheme. Appendix 2 contains a memorandum by the Government Actuary on the finance of the proposals.
PART I
CHAPTER 1
THE NEED FOR CHANGE

The financial position of pensioners today

9. There are about 7,000,000 people drawing national insurance pensions today. Until the middle 1960s, comprehensive information on the financial position of pensioners (apart from those receiving national assistance) was lacking, although independent research had provided evidence that a substantial number were entitled to receive national assistance but had not applied for it. This evidence was confirmed by a survey which was carried out in 1965 by the Ministry of Pensions and National Insurance with the co-operation of the National Assistance Board. This survey indicated that while about 1,450,000 pensioners were being helped by national assistance, there were about a further 850,000 who could have qualified for some payment of assistance at that time but had not applied—and of these roughly 300,000 were living appreciably below national assistance standards. The survey also showed that a very large number were only just above national assistance levels. If those levels had been £2 a week higher, about three-quarters of all pensioners would have been within the scope of national assistance.

10. Since 1965 the Government have done much to improve the position of elderly people, by pension increases and in other ways. The new supplementary benefits scheme, which replaced national assistance in 1966, has increased the minimum standard of living guaranteed by the State; and many more people have been persuaded to claim. There are now about 2,000,000 national insurance pensioners dependent in some degree on supplementary benefit—over half a million more than benefited from national assistance. The supplementary benefits scheme has therefore improved the financial position of many of the poorest pensioners. But it cannot help those who are above supplementary benefit levels—even by only a few shillings. The rate rebate scheme which was introduced in 1966 brought extra help in its first year to some 800,000 elderly householders, covering about a million elderly people in all. Some of them were previously living below supplementary benefit levels; others had incomes only slightly higher. The extension of local authority rent rebate schemes has also benefited a

(1) This and other figures quoted in this chapter count a married couple as two, where both are over pension age and retired.


(3) "Financial and other Circumstances of Retirement Pensioners", H.M.S.O., 1966, pp. 83-85. Earlier the Committee of Enquiry into the Impact of Rates on Households had estimated that there were half a million retired householders apparently eligible for national assistance but not getting it—Cmd. 2582, 1965, para. 370.
number of the poorest. There has thus been a definite improvement in the lot of elderly people most in need. But it is still true that most pensioners have incomes around, or not far above, supplementary benefit levels.

11. Nearly a third of all pensioners are widows. This is the poorest group among the elderly. Nearly half of these widows receive supplementary benefit compared with about a fifth of other pensioners. It is likely that, if the level of supplementary benefit were raised by £1 a week, well over 80 per cent of widow pensioners over 60 would be eligible for it.

12. It is estimated that about half the total income of pensioners comes from national insurance pensions and supplementary benefits, and that their average income is around two-thirds of that of the rest of the population (counting children as a half). The general standard of living of pensioners is therefore substantially below that of the working population.

The Beveridge plan

13. How has it happened that the present scheme of national insurance, founded on the principles of the Beveridge Report(1), fails to provide an adequate income in retirement? In 1948 the Report seemed a great step forward for Britain and a model for many other countries. Our “Welfare State” became more comprehensive than that of any other country. Virtually the whole population was covered by national insurance and by the National Health Service.

14. The Beveridge plan was “first and foremost, a plan of insurance—of giving in return for contributions benefits up to subsistence level, as of right and without means test, so that individuals may build freely upon it”(2). It was based firmly on the contributory principle: benefits had to be earned. “Benefit in return for contributions”, Beveridge wrote, “rather than free allowances from the State, is what the people of Britain desire . . . Payment of a substantial part of the cost of benefit as a contribution irrespective of the means of the contributor is the firm basis of a claim to benefit irrespective of means”(3). It was based also on the principle of insurance in the sense that risks had to be pooled. “Each individual should stand in on the same terms; none should claim to pay less because he is healthier or has more regular employment”(4). Social insurance “implies a pooling of risks except so far as separation of risks serves a social purpose”(5).

15. The aim of the plan was “to make want under any circumstances unnecessary”(6). Beveridge condemned the inadequacy of the benefit provided by earlier social insurance schemes. The remedy he proposed was to improve social insurance “in three directions: by extension of scope to cover persons now excluded, by extension of purposes to cover risks now excluded, and by raising the rates of benefit”(7). . . . “Social Insurance should aim at guaranteeing the minimum income needed for subsistence”(8).

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(1) Social Insurance and Allied Services, Cmd. 6404, 1942.
(2) Ibid. para. 10.
(3) Ibid. para. 21.
(6) Ibid. para. 17.
(7) Ibid. para. 12.
(8) Ibid. para. 27.
The need to supplement this minimum with national assistance would eventually be wholly exceptional. While benefits other than pensions would start at a full "subsistence" level, the level of pensions was to be gradually increased over twenty years until eventually they too were adequate for "subsistence".

The national insurance scheme

16. The principles laid down by Beveridge were widely acclaimed at the time and were accepted as the basis for the planning which led up to the National Insurance Act of 1946. Yet it is clear in retrospect that the national insurance scheme, as it has developed over the last 20 years, has failed to achieve Beveridge's main objective—adequate pensions and other benefits by right of contributions.

17. The basic reason for this failure was undoubtedly the acceptance—which was almost unanimous—of Beveridge's recommendation that the scheme should be based on a system of flat-rate contributions and benefits; but there were four other factors—

(a) In the first place there was the increasing proportion of the population over pension age. This had been foreseen by Beveridge, but his method of dealing with it was not adopted. He had envisaged that twenty years after his scheme had started, when the first full pensions would be paid, the taxpayer would contribute nearly half the cost of the scheme. In practice, successive Governments have been reluctant to enlarge the Exchequer contribution to anything approaching this extent, as they considered that the cost of an insurance scheme should fall predominantly on the contributors.

(b) Secondly, the Government decided that existing pensioners should receive the full rate of pension straight away. Thus from 1948 the same level of benefits was given to all—pensioners, the sick, the unemployed and other categories. Furthermore, the decision was taken to offer full pensions to those approaching pension age after only ten years of contributions (to be paid between 1948 and 1958). These two concessions, although inescapable in the circumstances of the time, further weakened the financial foundations of the Beveridge scheme.

(c) Thirdly—and this was only dimly envisaged in the 1946 Act—there was a continuing need to improve the real value of pensions and to keep them moving upwards in step with the rising living standards of those in work.

(d) Fourthly, when the national assistance scheme came into operation in 1948 its levels (including allowances for rent) were in most cases substantially above the level of national insurance pensions and benefits. From the start, therefore, hundreds of thousands of old people needed to supplement their national insurance pension with an allowance from the National Assistance Board. Supplementation had become the rule for those with little or no other income—not, as was Beveridge's ultimate objective, the exception. This situation has persisted ever since.
18. Underlying these factors was the basic weakness of the flat-rate system itself. A flat-rate contribution falls equally on the incomes of rich and poor. It is easily borne by the better-off, but hits the poorest hardest. The flat-rate contribution had to be set, therefore, at a level which the lowest wage-earner could afford. Experience has shown that under this system the level of contribution necessary to provide adequate pensions would place too great a burden on the lowest-paid contributors. As already indicated, the alternative of placing the extra burden on the Exchequer was rejected by successive Governments. Nor were they prepared to adopt the course followed in some other countries of financing adequate pensions out of much higher employers’ contributions, because of the unacceptable effect on prices and the cost of living.

19. These were the problems which led to the introduction of the graduated pension scheme in 1961. The immediate purpose of this scheme was to find a new source of contribution income to buttress the ailing finances of national insurance. But the relief it provides to the finances of the flat-rate scheme is inherently limited; and in any case it does not tackle the long-term problem. Further, the grafting on to the flat-rate scheme of a separate structure of graduated contributions and pensions has created extra work for employers and made the system more difficult for people to understand.

20. The pensions provided in return for graduated contributions, combined with the flat-rate pensions, still offer no prospect of achieving the original objectives of the Beveridge plan. The graduated pension scheme fails in two respects: its pensions are left unprotected against inflation and it cannot be adjusted for economic growth. This failure was ensured by the form of contracting out which was adopted (see paragraphs 127 and 128). Employers can hardly be required to increase the occupational pensions of those who have been contracted out, to match improvements in the graduated pensions of the State scheme; and it would not be right to provide higher graduated pensions only for those who have not been contracted out.

21. Meanwhile, the cost of pensions continues to grow, if only because the number of pensioners is rising—at present at a faster rate than the number of contributors. In 1948 there was one pensioner for every 5.6 people at

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(1) The population of working age comprises men and women over minimum school-leaving age and below pension age (65 for men, 60 for women). The numbers take account of the Government’s decision to raise the school-leaving age in 1972-73.
work. At the end of 1967 there was one pensioner for every 3.6 people at work. By 1980 it is estimated that there will be one pensioner for every 3.2 people at work. As Table 1 shows, between 1967 and 1980 the proportion of the population over pension age is expected to increase from 15.5 to 16.2 per cent. Between the same two years the ratio of people over pension age to the population of working age is expected to increase from 25.3 to 28.3 per cent. Later on, the proportion of those over pension age is expected to decline.

Conclusion

22. Neither the flat-rate scheme by itself, nor the present combination of flat-rate and graduated schemes, has succeeded in providing adequate pensions by right of contribution. For those without occupational pensions or private means, it is not the national insurance scheme which provides security in old age, but the supplementary benefits scheme. The latter is not, as was intended, just a "safety net" for the exceptional case. Instead it is a vast platform which now helps to support some two million people over pension age.

23. Like the original flat-rate scheme as planned in the Beveridge Report, the present scheme is static, and the existing structures of both benefits and contributions have failed in their purpose. The only real way forward, which tackles the problem at its roots as well as having great merits of its own, is to create a comprehensive scheme of fully earnings-related benefits and contributions, as described in the following chapters.
PART II

CHAPTER 2

BASIC OBJECTIVES

24. The scheme now proposed will have the following basic objectives—

(1) Rights to benefit must be earned by the payment of contributions.

(2) Benefits and contributions must be related to the contributor's earnings.

(3) Benefits must normally be sufficient to live on without other means.

(4) Benefits must take into account changes both in price levels and in general living standards.

(5) Women will contribute on the same basis as men and earn similar benefits.

(6) The scheme will be run on the "pay-as-you-go" principle.

(7) The State scheme will work in partnership with occupational pension schemes.

(8) People changing their employment will be legally entitled to have their occupational pension rights preserved.

(1) Rights to benefit must be earned by the payment of contributions

25. It is as true today as when Beveridge wrote his Report that benefit in return for contributions is what the people of Britain desire; and the State has already undertaken obligations to those who have paid contributions, often for very many years. These obligations have to be honoured. The present annual cost of retirement pensions alone is over £1,500 million, which is equivalent to 5s. 3d. on the standard rate of income tax. Even if it were remotely realistic to consider a transfer of this order from contributions to taxation, the Government would still think it wrong for pensions to be wholly tax-financed. People do not want to be given rights to pensions and benefits; they want to earn them by their contributions. Moreover, the level of wholly tax-financed pensions would undoubtedly be low. This is because people are prepared to subscribe more in a contribution for their own personal or family security than they would ever be willing to pay in taxation devoted to a wide variety of different purposes.

26. For all these reasons the Government reaffirm their commitment to the contributory principle. The success of the new scheme must not depend on the willingness of future Governments or future generations of taxpayers to prop it up with an increasing proportion of support from the Exchequer. The same share of the scheme's income will come from the taxpayer as at present, and this proportion should never need to be changed. In every year the major part of the scheme's income must come from contributors and their employers.
(2) Benefits and contributions must be related to the contributor's earnings

27. The principle of relating benefits to the individual contributor's earnings, and so to his standard of living while at work, is already widely accepted in the social security schemes of other countries. Although most people are reconciled to some drop in their living standards at retirement, there is a limit to the reduction which is felt to be tolerable in any particular case. Where earnings at work have been low there may be little, if any, margin for a lowering of standards. Better-off people will have a greater margin, but will have developed a pattern of habits and expectations which, while capable of some adjustment, can only be abandoned at great psychological and social cost. People choose their housing according to what they have been accustomed to afford; they incur, therefore, not only expenditure on such things as rent, rates and repairs, but also other expenditures arising from the community in which they live—for example, on participation in local activities. Retirement is in itself a difficult time of social and psychological adjustment. For all these reasons, pensions need to be related to the previous earnings of the pensioner.

28. About three-quarters of the members of occupational pension schemes are in schemes which are earnings-related. This is clearly the trend and is what more and more people are coming to expect from a good pension scheme. This makes it all the more important that the State scheme itself should be based on the principle of earnings-relation. If it were to be kept basically flat-rate, retired people would continue to be divided into two nations—those with good occupational superannuation, and those with little or nothing to add to their basic State pension except supplementary benefit based on a test of means and needs.

29. The principle of earnings-related benefits means, in turn, that contributions must be earnings-related as well. Payment of higher benefits to those with higher earnings cannot be justified unless they have paid, and are known to have paid, higher contributions to the scheme. Earnings-related contributions also have great advantages in themselves. They enable the total income of the scheme contribution to be increased, and to be made automatically buoyant in that it rises as earnings levels rise. At the same time the burden on contributors with low earnings can be reduced. This has particular importance for people who work at low rates of pay or cannot manage a full working week.

30. Earnings-relation does not mean, however, that the State scheme will be extended to cover the whole of a person's earnings, however large. Many people would consider compulsory State pension provision justified only up to a certain point. As explained in paragraphs 45 to 48, the State scheme will continue to leave sufficient room for occupational pension schemes. Indeed, superannuation is only one way of providing for old age, and some people will prefer to make part of their provision by buying their own homes, or by investment. These are all reasons why there should be a maximum to the State pension and in consequence an annual earnings "ceiling" above which employees are not required to pay further contributions.

(3) Benefits must normally be sufficient to live on without other means

31. It might seem at first sight that, as in some occupational schemes,
pensions under the new scheme should be the same percentage of earnings at all levels up to the scheme's ceiling. But if this percentage were set high enough to ensure adequate pensions for low earners, the cost of applying it uniformly up to the ceiling would be very great, and the contributions needed to finance the scheme would be much too high. State provision at this level for the middle and higher earner would not be justified. The scheme must therefore strike a balance. It must provide adequate pensions at all levels, but without requiring excessively high contributions. This will be achieved by a pension formula which gives greater weight to the contributions paid on the first third of earnings covered by the scheme.

(4) Benefits must take into account changes both in price levels and in general living standards

32. Beveridge could not foresee, or allow for, the great economic changes which have taken place even over the quarter of a century since he wrote his report. A pension scheme spans not just a quarter of a century but the whole of adult life. For the individual there will be some forty to fifty years during which rights to pension are earned, followed by, in many cases, twenty years or more during which pension is drawn. Among risks which must be pooled is the risk that money will change its value. Among needs which must be met is the need for pensioners to share in the nation's rising living standards. In 1908 the 5s. pension was seen as a great step forward. Sixty years later a pension of eighteen times this amount is still not enough to live on without other means.

33. For these reasons the new scheme must meet two separate requirements. First, when pensions come to be awarded they must reflect changes in general earnings levels which have taken place during the contributor's working life. Secondly, pensions in payment must be adjusted regularly for further economic changes which take place during retirement. In both cases adjustment is needed not only for changes in price levels but also for changes in general living standards. (The application of this principle is discussed in paragraphs 68 and 100 to 103). The importance of adjusting for both factors can be seen by looking back at what has actually happened in the past. In 1922 the average earnings of adult men were about £3 a week. In April 1968 they were over £22 a week. Only part of this increase was needed to compensate for rising prices. Earnings of about £10 would buy today what the worker could have bought with earnings of £3 in 1922. Thus while prices have more than trebled over this period, the real purchasing power of average earnings has more than doubled.

34. The new scheme will accordingly provide a "dynamic" pension, earned by the individual's contributions on his earnings over working life but with his record in each year re-valued according to subsequent changes in earnings levels generally, up to the time he reaches pension age. This will ensure that the earnings figure from which his pension is calculated—and so the pension itself—is in line with general living standards at the time he reaches pension age. Further regular adjustments will then be made to the pension during the years of retirement. Those at work are in a position to use their bargaining strength to increase their share of the nation's income. Pensioners do not have the power to protect their interests in this way.
Women will contribute on the same basis as men and earn similar benefits.

35. The new scheme, like the present one, must take account of family needs. Some wives are away from paid work for long periods looking after their families. Furthermore, among married women who will reach pension age in the next twenty or thirty years, even those who have spent substantial periods at work will often have achieved no corresponding insurance record, since under the present scheme they are able to choose not to pay the flat-rate contributions. Pensions and other benefits based on their husband's records will therefore still be needed both for married women and for widows. But at the same time those who do go out to work must be enabled to earn benefits in their own right, and must expect to pay their fair share towards a scheme which pools risks and depends on contributions based on earnings.

36. Under the present scheme, a married woman usually obtains a relatively unfavourable return for such contributions as she has paid. Not only does she normally receive a reduced personal rate of flat-rate sickness or unemployment benefit, but she may gain no extra pension from flat-rate contributions she has paid before, or during, her marriage: if her husband has retired or has died, she receives no pension from her own flat-rate contributions unless they have been sufficient to earn more than the amount for which she qualifies in any case on his record.

37. This is one reason why married women are at present offered an option whether or not to pay flat-rate national insurance contributions. A second reason for the option is to prevent a serious disincentive to their undertaking part-time work. Normally a person who works for more than eight hours a week is liable to pay the full flat-rate contribution. This can take a very large slice out of part-time earnings. Many married women contemplating part-time work would wonder if it was worth while to work at all if, on top of the costs of travel to work, clothing and so on, they were obliged to pay the flat-rate contributions. Under the new scheme, this reason for providing a contribution option will disappear. Married women in part-time employment, like other employees, will be able to contribute according to their earnings. Those who earn little will pay little. It will no longer be necessary to face them with the choice of either paying a contribution which represents an unduly large proportion of earnings, or else opting out of both the contribution and the benefits.

38. The new scheme must recognise that it is now very common for married women to go out to work. In 1931 less than a million did so. By 1951 the number had risen to more than 2½ million. Now it exceeds 4¾ million. For the combined pensions of a married couple who have both worked to reflect the standard of living achieved by their joint efforts, they must be based on the earnings of both husband and wife.

39. Under the new scheme women who go out to work, whether they are single, married or widowed, will contribute on the same basis as men, and will earn pensions and other personal benefits in their own right. When they are sick or unemployed, married women will receive the same personal rate of benefit as single men and women with the same earnings. They will also be entitled to have their pensions calculated on their earnings in the same way as single people. But for wives who, for one reason or another,
do not have a substantial record of their own, a pension on their husband’s record will continue to be provided. For widows, the right which will be given to older widows to inherit their husband’s full rate of earnings-related pension will be one of the new scheme’s most beneficial features.

40. Besides its pension provisions, the new scheme, like the present one, will include benefits for widows of working age. These benefits will be based on the earnings record of the husband, and will be available to widows with children and to childless widows above a certain age.

41. It is often suggested that the national insurance scheme should go further and cover either all “fatherless families” or at least the children in such households: this would mean an insurance benefit for divorced, separated and unmarried mothers. “Fatherless families” as a whole, however, not only divide into obvious groups but also show wide variations of need and circumstances within each group. There is a great difference between the needs of an unmarried mother who supports her child alone, and those of another girl who has a stable relationship with her child’s father; and there are many possible gradations between these two extremes. Similarly, it is often very difficult to distinguish between temporary separations and marriages that have finally broken down. Again, the father of the children is normally liable to contribute towards their maintenance, while he may or may not be liable for the maintenance of the mother. Whatever the extent of his liability, he may or may not be honouring his obligation. The available information about the numbers, structure and needs of these families is very inadequate.

42. Social security benefits are one obvious method by which fatherless families can be helped by Government action, and many of them are already receiving supplementary benefits. But they are also affected by the law on family matters and the practices of the courts (on which the Graham Hall Committee(1) have recently made a valuable contribution) and by central and local Government policies, especially policies on housing, education and child care. The Government have therefore decided, first, to start a further study(2) of the circumstances of all families with children, paying special attention to one-parent families (whether fatherless or motherless); and, secondly, to appoint a committee to consider the general position of one-parent families in our society and whether there are further methods by which they should be helped. The results of the study mentioned above will be available to the committee, who will meanwhile proceed with other aspects of their work. The appropriate provision for one-parent families will be further considered when the results of the study and the committee’s report are available.

(6) The scheme will be run on the “pay-as-you-go” principle

43. As explained in paragraph 52, the new scheme will have two separate funds: a National Superannuation Fund and a Social Insurance Fund. Neither of them will be “funded” in the technical sense in which most occupational schemes are funded (see paragraph 47). Both funds will be run, like the present scheme, on the “pay-as-you-go” principle. This principle

(2) The results of a study made in 1966 were published under the title “Circumstances of Families”, H.M.S.O., 1967.
is that current contribution income is used to meet current benefit expenditure—the contribution rates for any period being accordingly fixed to meet the expected expenditure in that period(1). Thus contributions paid into the National Superannuation Fund will be used to finance current pensions expenditure. At the same time, the State will undertake to provide the contributors with pensions, calculated according to the new scheme's provisions, when they themselves come to retire. The cost of these future pensions will in turn be met from contributions paid at the time. Since the new scheme's contributions will be earnings-related, the income they produce will automatically rise with the higher earnings levels which can be expected to accompany economic growth. In this way the new scheme, with its earnings-related contribution income, will be able, without imposing an excessive burden on future generations of contributors, to give pensioners and other beneficiaries not only protection against the effects of price increases but also a share in the general improvement of the nation's living standards. (See chapter 7.)

44. While “pay-as-you-go” financing means that the money currently being contributed for pensions is paid out to the existing pensioners, each contributor will at the same time be building up rights to his or her own personal pension. The new pensions will be personal in the sense of being related to the individual contributor's own earnings record, instead of being at a uniform rate as under the present flat-rate scheme. They will also be personal in that rights earned will be retained regardless of changes in employment, whatever the reason for them. (Universal transferability of pension rights on change of employment is not practicable for occupational schemes—see chapter 6.) Contributors will be given a regular report from the Department of Health and Social Security on their record under the new scheme.

(7) The State scheme will work in partnership with occupational pension schemes

45. As a result of the growth of occupational pension schemes in recent years, described in chapter 5, people will increasingly become entitled to superannuation consisting of two parts—one part from the State scheme and the other from an occupational scheme. For them the State scheme will serve as a foundation for the type of provision which occupational schemes are most suited to provide.

46. Occupational pension schemes have an important part to play in partnership with the State scheme. This partnership cannot consist, however, of a division of the population into two sectors of pensioners, State and occupational. It would be extremely difficult to apply any such division to people who move into and out of occupational schemes at different stages of their working lives. The best foundation for the success of occupational schemes is the existence of a substantial basic compulsory State scheme; and strong arguments can be advanced that, so far from handicapping occupational schemes, the new State scheme will assist their development. (See paragraphs 106 to 109.)

(1) In the early years of the new scheme, the income of the National Superannuation Fund will be somewhat more than will be needed to meet its current expenditure—see paras. 167 to 170.
47. The strength of occupational pensions lies in the principle of savings upon which most of them are built. The contributions paid to private schemes accumulate and earn an element of interest which grows throughout the working life of the member. This interest contributes an important part of the pension when it comes to be paid out. A "pay-as-you-go" scheme operated by the State—whether a nation-wide scheme like national insurance or a sectional scheme such as is provided for civil servants—is not obliged to accumulate a fund except in so far as may be necessary to provide a reserve against any unexpected drop in income or rise in expenditure. Its income from interest accordingly plays a comparatively small part in meeting its benefit expenditure.

48. While a State scheme must have relatively standardised provisions, an occupational scheme can be adapted to meet the special needs of particular occupations and industries. Inevitably the major changes in the State scheme which the Government are proposing will involve readjustment in occupational provision. The extent of the readjustment required can be limited by an arrangement for partial contracting out of the State scheme, as explained in chapter 5. On the other hand, during the past few years the growth of occupational provision may have been held back in some cases while the Government's proposals were awaited. The Government hope that the publication of this White Paper will enable further development in such cases to go ahead.

(8) People changing their employment will be legally entitled to have their occupational pension rights preserved

49. At present there are no universal or comprehensive arrangements for safeguarding occupational pension rights on changes of employment. A Committee of the Minister of Labour's National Joint Advisory Council, which was appointed to report on the economic and social implications of existing arrangements for preservation of pension rights on change of employment, concluded that there were strong social arguments for more extensive arrangements for safeguarding occupational pension rights(1).

50. The Government endorse this conclusion and accordingly intend to impose on all occupational schemes the obligation of offering to their members the right, if desired, to have their pension rights preserved on change of employment. Those employees who prefer to have their contributions returned to them will however still be able to do so. (See chapter 6.)

CHAPTER 3

THE GOVERNMENT'S MAIN PROPOSALS

51. This chapter describes the Government's main proposals. Fuller explanations of certain points are given in Appendix 1. For convenience all cash figures are expressed in pounds, shilling and pence, rather than in the decimal currency which will come into use before the new scheme begins.

THE NATIONAL SUPERANNUATION FUND AND THE SOCIAL INSURANCE FUND

52. At present there is one fund for all national insurance contributions and benefits. Under the new scheme there will be two separate funds: a National Superannuation Fund for pensions, widowedness benefits and death grant; and a Social Insurance Fund for the remaining benefits. Each fund will receive its appropriate share of the total income from contributions, and this share will be used to meet the expenditure on the benefits charged to it (including benefits still in payment from the present scheme). Separate funds will reflect the different natures of the benefits concerned, and will help people to understand the purposes for which they are contributing. Contributions paid into one fund will not be diverted for use by the other. Contributors can therefore know what proportion of their contributions is for national superannuation and what proportion for other purposes, and can be sure that money paid for one purpose will not be used for another.

53. The initial rates of contribution to the National Superannuation Fund will be fixed with the aim of providing an income sufficient to meet the growing pension expenditure for some years after the new scheme begins. After that, the contribution rates will need to be somewhat increased. In the early years the National Superannuation Fund will accumulate a surplus, which will be invested. (See paragraphs 167 to 170 and the Memorandum by the Government Actuary at Appendix 2.)

CONTRIBUTIONS FOR EMPLOYED PERSONS

Employees' contributions

54. The present contributions for employed persons are in three parts. First, there is the flat-rate contribution, which is collected through the stamped card system. Secondly, there is the contribution for graduated pension, charged at 4½ per cent on earnings between £9 and £18 a week. Thirdly, there is the contribution for earnings-related short-term sickness, unemployment and widowedness benefits, charged at ½ per cent on earnings between £9 and £30 a week. The last two contributions are collected together through the PAYE income tax system.

55. Under the new scheme these three contributions will all be abolished, and with them the present system of stamped cards. Instead, all employees
coming within the PAYE system\(^{(1)}\) will pay a single type of contribution, collected through that system\(^{(1)}\). This contribution will be a straight percentage of all their earnings in each year\(^{(1)}\), up to a maximum or “ceiling” of about 1\(\frac{1}{2}\) times national average earnings\(^{(1)}\). At April 1968\(^{(1)}\) earnings levels this ceiling would be £1,700 a year (equivalent to about £33 a week); the cash amount will increase over the years as national average earnings rise. In 1968, about 7 per cent of the 22 million employees covered by PAYE were earning £1,700 a year or more, and so would have paid the new contributions on their yearly earnings up to that amount but not beyond. The remaining 93 per cent would have paid the new contributions on the whole of their earnings.

56. The percentage contributions will be paid by employed men and women alike. The percentage rate will be the same for both; and the new contributions (unlike the present flat-rate contributions) will be compulsory for married women and widows who go out to work, on the same basis as for other employees. At the start of the scheme the total contribution rate payable by employees will be 6\(\frac{1}{2}\) per cent. Of this total, 4\(\frac{1}{2}\) per cent will be for national superannuation. The remaining 2 per cent will be for social insurance benefits, industrial injuries benefits and a contribution to the National Health Service.

57. To illustrate how the change to the new contributions will affect employees, Table 2 shows the position as it would have been if the new scheme had started in April 1968\(^{(5)}\). The table gives, at various earnings levels, the total present-scheme contributions which were paid by employees at that time, their total new-scheme contributions, and the difference between the two. The corresponding figures when the new scheme starts will of course depend on the levels of earnings and of present-scheme contributions at that time.

\[^{(1)}\] Generally speaking, people who are treated as employed persons for national insurance purposes also come within the PAYE system, and vice versa. The possibility of bringing the two systems still closer into line is being examined. For employees with low earnings, see para. 99.

\[^{(2)}\] See Appendix 1, paras. 5 to 7.

\[^{(3)}\] See Appendix 1, paras. 3 and 4.

\[^{(4)}\] Here and elsewhere, “national average earnings” is used, for convenience, to mean the average earnings of adult male manual workers in manufacturing industries and certain non-manufacturing industries and services, as obtained from the Department of Employment and Productivity’s half-yearly enquiries into earnings. The latest available figure (for April 1968) is about £22 5s. a week.

\[^{(5)}\] Because of the link with the PAYE system, the new contributions must begin on a 6th April, at the beginning of a “tax year”.

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TABLE 2
Employees' contributions

Total present-scheme and new-scheme contributions (including amounts for the industrial injuries scheme and the National Health Service) at April 1968 levels, paid by employees (not contracted out).

<table>
<thead>
<tr>
<th>Level of weekly earnings</th>
<th>Present scheme</th>
<th>New scheme</th>
<th>Change in contributions</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(1)</td>
<td>(2)</td>
<td>(3)</td>
</tr>
<tr>
<td></td>
<td>Employee's total weekly contributions (flat-rate plus graduated)</td>
<td>Employee's total contributions (expressed as weekly rate)</td>
<td></td>
</tr>
<tr>
<td></td>
<td>s. d.</td>
<td>s. d.</td>
<td></td>
</tr>
<tr>
<td><strong>MEN</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>£11 (½ national average)</td>
<td>17</td>
<td>14</td>
<td>-3</td>
</tr>
<tr>
<td>£16 10s. (¼ national average)</td>
<td>23</td>
<td>22</td>
<td>9</td>
</tr>
<tr>
<td>£22 (national average)</td>
<td>24</td>
<td>29</td>
<td>+5</td>
</tr>
<tr>
<td>£27 10s. (1¼ national average)</td>
<td>25</td>
<td>37</td>
<td>+11</td>
</tr>
<tr>
<td>£33 (1½ national average) or more</td>
<td>25</td>
<td>44</td>
<td>+19</td>
</tr>
<tr>
<td><strong>WOMEN</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>£8</td>
<td>13</td>
<td>10</td>
<td>-2</td>
</tr>
<tr>
<td>£11</td>
<td>15</td>
<td>14</td>
<td>-1</td>
</tr>
<tr>
<td>£16 10s.</td>
<td>20</td>
<td>22</td>
<td>+1</td>
</tr>
<tr>
<td>£22</td>
<td>22</td>
<td>29</td>
<td>+7</td>
</tr>
<tr>
<td>£27 10s.</td>
<td>22</td>
<td>37</td>
<td>+14</td>
</tr>
<tr>
<td>£33 or more</td>
<td>22</td>
<td>44</td>
<td>+21</td>
</tr>
</tbody>
</table>

The figures for women in column (2) are for those contributing under the present flat-rate national insurance scheme. For married women and widows who have opted not to do so (and who therefore pay only the industrial injuries contribution of 7d. a week) the figures in column (2) would all be 12s. 7d. less; and 12s. 7d. would therefore need to be added to the figures in column (4).

Employers' contributions

58. Employers' contributions under the new scheme will be calculated as a percentage of their total PAYE payroll, with no earnings ceiling(1). At the start of the scheme, the total contribution rate for employers will be 6½ per cent. Of this total, 4½ per cent will be for national superannuation; this will yield approximately the same total income as the employees' rate of 4½ per cent, which will apply only up to the earnings ceiling. Employers and employees as a whole will therefore contribute approximately the same to the National Superannuation Fund. Of the remaining 2¼ per cent of the employers' contribution rate, 2 per cent will be for social insurance benefits, industrial injuries benefits and a contribution to the National Health Service; and ¼ per cent has been allowed for the Redundancy Fund (replacing employers' present flat-rate contributions to that fund). The contribution to the National Health Service will be at the same percentage rate for employers as for employees (in the former case without an earnings ceiling); this is in contrast to the present flat-rate National Health Service contributions, which are much lower for employers than employees.

The Exchequer contribution

59. The total Exchequer contribution to the present national insurance scheme is now about £340 million a year; this amounts to about 18 per cent of the combined national insurance contributions of insured persons

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(1) See Appendix 1, paras. 8 to 10.
and employers. Under the new scheme the Exchequer will contribute approximately the same proportion; and the amount this produces will increase automatically as earnings levels rise.

**NATIONAL SUPERANNUATION BENEFITS FOR EMPLOYED PERSONS**

Retirement pensions

Pension ages and the retirement condition

60. The minimum ages for pension will remain at 65 for men and 60 for women(1). The pensions will still be retirement pensions: that is, until age 70 (men) or 65 (women) they will be paid only to people who have retired from regular employment. Up to these ages there will therefore still need to be an earnings rule, whereby a retirement pension is reduced if the pensioner earns more than a certain amount(2). Those who retire after age 65 (men) or 60 (women) will earn extra pension, the amount of which will take into account both the contributions they have paid after reaching pension age and the amount of pension they have forgone through their later retirement.

Transition to the new-scheme rates

61. Rights to the full new pensions will be built up gradually over the first twenty years of the scheme. Pensions for people reaching pension age during this twenty-year “maturity period” will be at intermediate rates, calculated by combining rights earned by contributions under the present flat-rate scheme with rights earned under the new scheme. Those who reach pension age after the first year of the new scheme will get nineteen-twentieths of the present-scheme rate, plus one-twentieth of the the new scheme rate based on their earnings since the new scheme began. Those reaching pension age after the second year will get eighteen-twentieths and two-twentieths respectively. And so on, until the first fully mature new-scheme pensions are paid to those reaching pension age twenty years after the scheme begins. The pensions awarded during the maturity period will remain at intermediate rates; but the rates in payment will be reviewed every two years as described in paragraphs 100 to 103. The transitional arrangements are explained in more detail in Appendix 1, paragraphs 20 to 23.

End of the present graduated scheme

62. When the new earnings-related scheme begins, the present graduated scheme will come to an end; and no further rights will be earned under it. The graduated pension rights already earned up to that date will be preserved, and paid on top of the new-scheme pensions calculated as in paragraph 61. For the reason explained in paragraph 20, the amounts earned under the present graduated scheme will not be covered by the two-yearly reviews of benefit rates.

How new-scheme pensions will be calculated

63. The principles on which the new pensions will be calculated were set out in chapter 2. The following paragraphs show how these principles will be put into practice.

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(1) This important decision is explained in Appendix 1, paras. 11 to 15.
(2) See Appendix 1, paras. 16 to 19.
(i) The main pension formula

64. The pensions earned under the new scheme will, like the contributions, be wholly earnings-related. The fully mature new-scheme pension for a single person will be made up of 60 per cent of his or her earnings up to half national average earnings, and 25 per cent of the remainder up to the scheme's ceiling. This is the new scheme's main "pension formula". At April 1968 earnings levels, the changeover point between the two parts of the formula would have been at earnings of about £11 a week, and the ceiling at earnings of about £33 a week. Both the changeover point and the ceiling will increase as national average earnings rise.

65. Rights built up by contributions under the present flat-rate scheme will be taken into account in calculating new-scheme pensions, as explained in paragraph 61. Contributors with very low earnings under the new scheme, or none at all, will be able, if they wish, to keep up their right to pension at the rate provided for present-scheme pensioners (see paragraph 99).

(ii) Earnings over working life

66. Under the present scheme, both the flat-rate and the graduated pension entitlement depend on the contributions paid during the whole of working life. On the other hand, many occupational schemes calculate pensions on earnings during the last few years of employment. This is appropriate for schemes which cover only salaried workers who can expect to reach their peak earnings just before they retire. But it would not be suitable for many manual workers. In many occupations the earning ability of manual workers drops in their forties and fifties because they can no longer do the more strenuous work, or can no longer work at the same pace. Taking account of all earnings throughout working life is fairer both to people who have been relatively high earners at different periods of their lives and to those who have had to take work of a lower grade at any time for health or other reasons. Retirement pensions will therefore continue under the new scheme to be based on the "whole life" principle. The working life for this purpose will be taken as the period from the beginning of the tax year containing the 19th birthday, up to age 65 (men) or 60 (women).

67. The present flat-rate scheme requires a person to have a minimum life average of 13 contributions a year in order to qualify for any pension (apart from a pension received by a wife or widow on her husband's record). There will be a corresponding minimum qualifying condition under the new scheme.

(iii) Life average earnings

68. When a contributor's life average under the new scheme comes to be calculated, his earnings in each year will be re-valued in line with the changes which have since taken place in the level of national average earnings. In this way his earnings will be converted into their up-to-date equivalent at the time he reaches pension age. As a result, for example, a man who had had exactly national average earnings every year of his working life would have his pension calculated on national average earnings as they were at the time he reached pension age, not on the money average of his actual
earnings over life (which might come to only a fraction of this, as the figures in paragraph 33 show). All the necessary recording and calculation will be done by computer.

(iv) Credited earnings for periods of sickness or unemployment

69. If pension were calculated only on actual earnings, adjusted as described above, people with considerable sickness or unemployment might not receive adequate pensions. During periods when sickness or unemployment benefit is paid, and in some other circumstances, contributors’ records will therefore be credited, for the purpose of calculating their future benefit entitlement, with earnings of, normally, half the national average (that is, about £11 a week at April 1968 levels). This will correspond to the full 60 per cent part of the pension formula, as described in paragraph 64. Further details of the arrangements for crediting earnings are given in Appendix 1, paragraphs 24 to 26.

(v) Examples of new-scheme pensions for a single person

70. Under a dynamic earnings-related scheme of this kind, it is not possible to foretell what a person’s eventual pension will amount to in cash terms. This will depend both on his own earnings record over working life and on changes in national average earnings during that time. Any example expressed in cash terms can therefore do no more than give a general idea of how the pension calculation will work in practice.

71. It is not possible to forecast what the level of national average earnings will be when the new scheme starts, or over the following years. The results produced by the pension formula are therefore illustrated in Table 3 by reference to the actual earnings levels in the recent past. The table gives some examples of fully mature new-scheme pensions (see paragraph 61) worked out at the earnings levels which existed in April 1968(1). These examples therefore illustrate the pensions which contributors reaching pension age at that time would have received if the new scheme had started twenty years previously, in April 1948. Figures are given for contributors with life average earnings of five different proportions of the national average(1), as shown in column (1). The cash amounts of these earnings at April 1968 levels are in column (2). The corresponding weekly pension amounts which the new scheme’s 60 per cent/25 per cent pension formular would produce for a single person are in column (3). The figures in this column represent the pension at the time of award, and show the effect of the greater weight given to earnings up to the changeover point of the formula (see paragraph 31). For married couples the pensions would be higher by at least £2 16s. (the wife’s flat-rate pension on her husband’s record), with the amount above this depending on the wife’s own record, as explained in paragraph 72. There will continue to be flat-rate increases for dependent children. Column (4) of the table shows for comparison the total present-scheme pension, flat-rate plus graduated, for a single man in April 1968. (The present graduated pension scheme started in April 1961; the amounts of graduated pension shown therefore represent the totals earned over that scheme’s first seven years.)

(1) See footnote on page 20.
**TABLE 3**

<table>
<thead>
<tr>
<th>Proportion of national average earnings achieved by pensioner during working life</th>
<th>Col. (1) at April 1968 earnings levels</th>
<th>Fully mature new-scheme pension at April 1968 earnings levels</th>
<th>Present-scheme pension in April 1968</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1)</td>
<td>(2)</td>
<td>(3)</td>
<td>Flat-rate</td>
</tr>
<tr>
<td>£ s.</td>
<td>£ s.</td>
<td>£ s.</td>
<td>s.</td>
</tr>
<tr>
<td>½ (changeover point in the pension formula)</td>
<td>...</td>
<td>11 –</td>
<td>6 12</td>
</tr>
<tr>
<td>⅔</td>
<td>...</td>
<td>16 10</td>
<td>8 –</td>
</tr>
<tr>
<td>1 (average)</td>
<td>...</td>
<td>22 –</td>
<td>9 7</td>
</tr>
<tr>
<td>1½ (the scheme’s ceiling)</td>
<td>...</td>
<td>27 10</td>
<td>10 15</td>
</tr>
<tr>
<td>33 –</td>
<td>12 2</td>
<td>4 10 + 9 = 4 19</td>
<td></td>
</tr>
</tbody>
</table>

(a) Earnings and pension figures are given in weekly rates, with earnings rounded to the nearest 10s. and pensions to the nearest shilling.

(b) The graduated pension amounts shown in column (4) are those for a man, whose earnings are assumed to have remained throughout at the proportion of the national average shown in column (1).

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**The new deal for women**

**Pensions for married women**

72. A married woman’s retirement pension will be calculated in whichever of the following ways is more favourable for her—

(1) A pension based on her own life average earnings and calculated from the main 60 per cent/25 per cent pension formula in exactly the same way as for men and single women (see paragraphs 64 to 71).

or

(2) A flat-rate pension on her husband’s record, as under the existing scheme (the present rate being £2 16s. a week), plus an earnings-related addition of 25 per cent of her own life average earnings.

73. At the start of the new scheme, calculation (2) will be better for the great majority of pensioner wives; but the build-up of married women’s earnings records under the new scheme will gradually increase the numbers for whom calculation (1) is more favourable. Under either calculation all the wife’s contributions paid after the new scheme begins, whether before or during marriage, will bring her extra pension. For dependent wives under age 60 a flat-rate addition to the husband’s retirement pension will be paid, as under the existing scheme (the present rate being £2 16s. a week).

74. The new earnings-related pensions for married women, like those for single people, will build up gradually, over the first twenty years of the scheme, to the fully mature new-scheme rates. Under calculation (1) in paragraph 72, the method will be as described in paragraph 61. Under calculation (2), the earnings-related addition for a married woman reaching pension age after the first year of the scheme will be one-twentieth of the earnings-related addition for a man of the same age (which will have been, under calculation (1), fully mature at pension age).

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(1) See Appendix 1, paras. 27 and 28.
full 25 per cent rate (calculated on her average earnings since the new scheme began); and the proportion will rise, by annual steps of one-twentieth, until the fully mature new-scheme rate is paid to those reaching pension age twenty years after the scheme begins.

Women widowed after reaching age 60

75. A wife whose husband dies when she is aged 60 or over will receive whichever of the following pensions is more favourable for her—

(1) The same personal rate of retirement pension as her husband was receiving, or had earned, when he died. If he died before reaching age 65, her pension will be based on his life record of average earnings, with the years he had still to live before reaching age 65 filled in by crediting earnings at, normally, one half the national average(1).

or (2) A pension based entirely on her own life average earnings and calculated from the main 60 per cent/25 per cent formula in the usual way.

Younger widows

(i) Widow's allowance

76. There will continue to be an earnings-related widow's allowance for the first six months of widowhood. As now, this will be based on the husband's earnings in the previous tax year. The method of calculating the allowance will be revised to take into account the abolition of flat-rate contributions and benefits.

(ii) Widowed mother's allowance

77. A widow who has a child under 19 in her family will receive an earnings-related widowed mother's allowance. This will be calculated in the same way as the pension in paragraph 75(1), with the addition of a flat-rate allowance for each dependent child. As at present, the amount of this allowance will be higher than child allowances generally.

(iii) Widow's pension

78. An earnings-related widow's pension will be paid to women who are widowed after reaching age 50, and also to widows who are aged 50 or over when their entitlement to widowed mother's allowance ceases. This pension will be calculated in the way described in paragraph 75(1). Any contributions of the widow after her husband's death will add to the eventual retirement pension which she will receive on his record. Alternatively, if better, her retirement pension will be based entirely on her own life average.

79. At present a woman who is widowed under age 50, and has no child under 19 in her family, normally receives no pension at all until she reaches age 60. The same is true of a widowed mother whose youngest child reaches 19 before she is 50. A difference of a few days in the date of the husband's death or in a child's nineteenth birthday can decide whether for the next ten years a widow receives a pension at the full rate or nothing at all.

(1) See Appendix 1, paras. 24 to 26.
80. Under the new scheme, a woman who is between age 40 and 49 when she is widowed, or when her entitlement to widowed mother's allowance ceases, will receive, while she is under age 60, an earnings-related widow's pension. This will be calculated in the same way as in paragraph 78 but scaled down according to her age at that time, with a minimum pension corresponding to about £1 10s. a week at present-day levels. Her eventual retirement pension will take into account both her husband's earnings record and any earnings of her own after his death. Alternatively, if better, her retirement pension will be based entirely on her own life average.

81. Existing widows will be able to qualify for a scaled-down flat-rate pension under the new arrangements, if they would have satisfied the new qualifying conditions at the time when they were widowed or when their entitlement to widowed mother's allowance ceased.

Transitional arrangements for widowhood benefits

82. The transitional arrangements for the widowhood benefits described in paragraph 77 to 80 will be similar to those for retirement pensions (see paragraph 61), with a gradual build-up, over the first twenty years of the scheme, to the fully mature new-scheme rates.

Pension provision for divorced women

83. Under the present flat-rate scheme, a woman who becomes divorced under age 60 can have her retirement pension calculated by taking over her ex-husband's contribution record for the period of their marriage, if this is to her advantage. Under the new scheme she will be able to take over his record for the period before as well as during the marriage.

84. A woman who becomes divorced after reaching age 60 can at present receive, on her ex-husband's insurance, the full amount of the flat-rate pension for a single person. A corresponding right will be given under the new scheme.

Pension provision for separated wives

85. The present scheme gives a separated wife cover for retirement pension and widowhood benefits on her husband's insurance, whether or not she herself has paid contributions. Her entitlement to these benefits on her husband's record will continue under the new scheme. Her rights will be made more valuable by the improvements in married women's pensions and widowhood benefits described in paragraphs 72 to 80.

Death grant

86. Death grant, which is paid to help with funeral expenses, will continue to be at a flat rate. The grant will be extended, on the insurance of close relatives, to cover the deaths of handicapped people who were living with them and who had never been able to work and contribute.

SOCIAL INSURANCE BENEFITS

Short-term sickness benefit

87. Under the present scheme, the basic flat-rate sickness benefit can be supplemented, for up to six months, by an earnings-related addition based on the employee's earnings in the previous tax year. In the new scheme
there will be a single earnings-related short-term sickness benefit, also payable for up to six months. There will continue to be higher rates for married men than for single people, and additions for children. Married women contributors who are themselves sick will receive the same personal rate of benefit as other contributors (instead of a lower rate as at present). During periods of benefit, earnings will be credited in the sick person's record, as described in paragraph 69. Further details of the new arrangements for short-term sickness benefit, including the benefit formula to be applied to the employee’s earnings, will be announced separately.

**Long-term sickness benefit**

88. After short-term sickness benefit ends, there will be a new earnings-related long-term sickness benefit. This will not be restricted to cases of permanent or prolonged illness, but will be the rate of sickness benefit paid after entitlement to the initial short-term rate has ended. It will therefore often be paid for comparatively short periods. For those who are not able to return to work it will be in effect an invalidity pension, which will continue until pension age and will then be replaced by retirement pension.

89. The rate of long-term sickness benefit will be calculated from the contributor's life average earnings in the same way as retirement pension (see paragraphs 64 to 69). The years remaining up to age 65 (men) or 60 (women) will be filled in by crediting earnings at, normally, one half the national average(1). Flat-rate increases will be paid for a dependent wife and children, as under the existing scheme. The transitional arrangements will be similar to those for retirement pensions (see paragraph 61), with a gradual build-up, over the first twenty years of the scheme, to the fully mature new-scheme rates.

**Attendance allowance for the very severely disabled**

90. Among those who have been ill or disabled for some time, there are a number with a handicap so severe that it makes them wholly or largely dependent on help from other people in coping with the ordinary functions of daily living. Where they are being cared for at home, the strain on their families can be considerable. Many of them prefer to remain in their own surroundings rather than go into a hospital or home; and many families are prepared to take on the extra burden of caring for a severely disabled relative.

91. A new attendance allowance will therefore be introduced for very severely disabled people. Wives who have not themselves been paying contributions will be able to receive the allowance on their husbands' insurance. The allowance will be at a flat rate, and will be available to people who are already disabled when it is introduced. A corresponding allowance will be provided under the supplementary benefits scheme; this will be of special help to those, such as the congenitally disabled, who have no contribution record and few resources of their own. The Government Social Survey is at present conducting a nation-wide survey of the chronic sick and disabled, sponsored by the Department of Health and Social Security. This is designed, among other things, to establish the facts which are needed before decisions are taken on the precise details of the new allowance.

(1) See Appendix 1, paras. 24 to 26.
Unemployment benefit

92. An earnings-related benefit, corresponding to the new short-term sickness benefit (see paragraph 87), will be paid for up to six months of unemployment. It will be followed, as under the present scheme, by a flat-rate benefit for up to a further six months.

Other benefits

93. Consequential changes in other insurance benefits, including maternity benefits and guardian’s allowance, and in industrial injuries benefits, will be announced separately.

OCCUPATIONAL PENSION SCHEMES

Partial contracting out of the new scheme

94. Employees in occupational pension schemes can be contracted out of the present State graduated pension scheme, but not out of the basic flat-rate scheme. The Government are confident that fair and workable arrangements can be made to allow employees in occupational schemes to be contracted out of part of the new retirement pension provisions. Under such arrangements the employee’s and employer’s contributions to the new scheme would be reduced, and part of the employee’s retirement pension would be provided instead by the employer through the occupational scheme. This subject is fully discussed in chapter 5.

Preservation of occupational pension rights

95. At present many employees in occupational pension schemes forfeit part or all of their pension rights when they leave a job. In future those who have satisfied certain minimum qualifying conditions will be given the right to have the amount of occupational pension which they earn preserved for them until they reach the age for drawing it. Those who prefer to have their contributions returned to them, when they change their employer, will still be able to do so. Further details are given in chapter 6.

Consultation on occupational pension matters

96. The Government will discuss the matters referred to in paragraphs 94 and 95 with representatives of occupational pension schemes and others specially interested in these subjects. In its role as employer, the Government will likewise be consulting the organisations representing employees in the public services.

THE SELF-EMPLOYED

97. Self-employed people are not included in the present graduated pension scheme. In principle their new-scheme contributions and benefits, like those for employees, should be related to their earnings. But thorough study of the problems has shown that this is not practicable, at least for the time being (see Appendix 1, paragraphs 29 to 32). The self-employed will therefore be brought into the new scheme by contributing to it at a flat rate. Someone with a mixture of employment and self-employment during his working life (as most self-employed people will probably have) will still have a single integrated record.
98. Self-employed men and women—including married women and widows, who at present can choose whether or not to pay contributions—will contribute alike. Their contributions will count for benefits (except, as now, unemployment benefit and industrial injuries benefits) at the level earned by employees with half national average earnings. This will correspond to the full 60 per cent part of the pension formula as described in paragraph 64. As with employed persons, there will be additional provision for wives and children. On this basis the total new-scheme contributions for a self-employed person would have come to about £1 7s. a week at April 1968 levels, of which about £1 1s. a week would be for the National Superannuation Fund. If the scheme had been introduced at that time, this would have involved increases of about 6s. a week for men and just under 10s. a week for women (or the full £1 7s. a week for those self-employed married women and widows not paying the present-scheme contributions). Contributions of this size would be a very heavy burden on those with low earnings. For this reason, the new self-employed contributions will be compulsory only for those earning more than half national average earnings (that is, about £11 a week at April 1968 levels). Those earning less than this will however be able to pay self-employed contributions if they want to; alternatively, they will be able to contribute voluntarily for pensions and certain other benefits (see Appendix 1, paragraphs 36-37). Ways in which the self-employed will be able to pay their contributions under the new scheme are being examined.

LOW EARNERS AND NON-EARNERS

99. Employees whose earnings are too low to bring them within the PAYE system (at present this means those earning less than £5 5s. a week) will not be compelled to pay contributions under the new scheme. Nor will people who do not earn at all. There will however be arrangements for voluntary contributions to be paid to bring a person’s record for any year up to the level which would produce a pension at the standard rate then in force for present-scheme pensioners (at present £4 10s. a week for a single person, £7 6s. for a married couple). Further details are given in Appendix 1, paragraphs 33 to 37.

REVIEWS OF PENSIONS AND OTHER BENEFITS IN PAYMENT

100. In the past there has been no proper system for increasing benefits already in payment. The intervals between increases have varied considerably, and the changes have rarely come into effect at what is clearly the best time of year, before the beginning of winter.

101. Under the new scheme the Government will be bound by statute to review every two years the main rates of national insurance and industrial injuries benefits in payment. The reviews will cover present-scheme(1) as well as new-scheme pensions and other benefits. The increases, which will always come into operation in the autumn, will compensate for any rise in price levels since the previous increase. But this inflation-proofing is only a minimum. Pensioners and other beneficiaries will also continue to share in the nation’s rising living standards. The actual amount of improvement

(1) Other than the present graduated pensions, for the reasons explained in para. 20.
on each occasion, beyond the inflation-proofing, must be left for decision by the Government of the day, which will need to take into account such factors as movements in earnings levels, changes in the standard of living of the community as a whole, and the general economic situation.

102. The Government propose that the benefit increases should be brought about by regulations, without the present need for a new Act of Parliament on each occasion.

103. As in the past, war pensions and allowances will be increased at the same time as other benefits; but no new statutory provision is needed for this since they are not governed by Act of Parliament. Supplementary benefits will be dealt with along with the main benefits in each biennial review; and they can always be increased by regulations.

TIMING OF THE SCHEME'S INTRODUCTION

104. The Government hope that the new scheme will be thoroughly discussed, in Parliament and elsewhere, before its details are finally settled; and they will consult organisations with special interests in this field. After taking account of these consultations, they intend to introduce the necessary legislation in the 1969-70 session of Parliament. Because of the link with the PAYE system, the scheme must start at the beginning of an income tax year, in April. The target date is April 1972.
CHAPTER 4

THE ALTERNATIVES

105. Before putting forward the proposals in the previous chapter, the Government have considered two other possibilities which are sometimes advanced as alternatives to extending the national insurance scheme: greater "selectivity", and reliance on occupational pension schemes.

Greater selectivity?

106. It is often suggested that, if national insurance pensions were to be kept at their present level, or were to be increased only to compensate for rising prices, greater help could then be given to the poorest pensioners. Giving larger pensions to those who do not "need" them is said to be wasteful. It is claimed that by being more selective the Government could reduce the burden of public expenditure. This amounts to suggesting that the present gap between contributory pensions and supplementary benefit should be widened, rather than narrowed.

107. In the Government's view there are compelling reasons why the main provision for social security should be through contributory benefits, rather than—as may be suitable in some other fields, such as rate rebates—through reliance on means-testing. The chief reasons are—

(1) A further widening of the gap between the levels of pensions and supplementary benefits could produce an enormous increase in the number of pensioners needing supplementation. As indicated in paragraph 9, in 1965 a widening of the gap by no more than £2 a week would have meant that something like three-quarters—that is, nearly five million—of all pensioners would have been within the scope of means-tested supplementation. This would be a disastrous step in the wrong direction. There is a widespread and deep-seated feeling that, after a lifetime of work, people should receive a pension which is not reduced because they have other income or savings. The figures just quoted show that by far the greater part of the expenditure on pension increases goes to people with low incomes.

(2) No means-tested scheme will be used by all those who are entitled to claim. The supplementary benefits scheme has shown that, with enlightened design and humane administration, much can be done to overcome ignorance or reluctance; but there will always be people in need who do not come forward. Either they are not reached by publicity about the scheme or, having treasured their independence throughout their working lives, they are reluctant to admit to outsiders, or sometimes even to themselves, that they find it difficult to make ends meet. This difficulty cannot be resolved by any magic of the computer, as some people have suggested. A computer can process efficiently and rapidly such facts as are fed into it. But it cannot make calculations on facts which have not
been collected. Inevitably those claiming supplementary benefit must answer what are commonly regarded as highly personal questions; and this is precisely what a minority are reluctant to do.

(3) Increased reliance on supplementary benefit in providing for old age would also have damaging effects on private savings and on occupational pension schemes. This point has been well expressed in a recent report by the State Pensions Committee of the National Association of Pension Funds:

"Employers are deterred from setting up schemes for lower-paid workers, if they see that much of the benefit to their employees will be counterbalanced by a reduction in the pensions provided from a State system to which they have contributed on the same basis as other less generous employers. Employees are reluctant to contribute to occupational schemes if they fear that a State means test will deprive them of much of the resulting benefit. Many employers are already finding that the means test for supplementary benefits under the present social security system is making it difficult for them to persuade their lower paid employees to join their pension schemes."(1)

108. The undesirable effects on the development of occupational schemes, and on savings generally, would occur whatever method of applying a means test was used. This alone rules out in this field any proposal based on the idea of a "negative income tax", which is sometimes put forward as a method of means-testing which is automatic and all-embracing, and therefore not open to social objections. But in fact a negative income tax would by no means be easy to operate. It is sometimes assumed that the Government already possess the relevant facts about people's requirements and current resources, and that all they need to do is bring together in a computer the different pieces of information held by different Departments. But this is far from true. For example, the Government do not have details of rents. Many elderly people with low incomes do not make a return to the Inland Revenue and can hardly be compelled to do so. The tax returns made by others cover income in the previous year—whereas up-to-date information would be essential if people's current needs were to be properly met.

109. All this reinforces the Government's determination to strengthen and develop the contributory principle in social security. People cannot be expected to contribute willingly for a pension unless it is worth having. The contributory principle would break down if many people had reason to believe that the Government would in the end pay the same amount whether they contributed or not.

Occupational pension schemes—an alternative for the longer term?

110. The second suggestion is that occupational pension schemes are becoming so widespread that eventually they could meet, or very nearly meet, all need for pensions above a low minimum provided by the State scheme. Some would go even further, seeking to combine this with the "selectivist" approach. They argue that the adoption of greater selectivity

(1) "The Future Relationship of State and Occupational Pensions", published by the National Association of Pension Funds, September 1968, p. 22.
in State pensions could pave the way for the ultimate withdrawal of Government from the field of provision for old age, except for a residual means-tested scheme. The State, it is suggested, could thus avoid incurring any pension obligations for those now starting work, and the savings could be split between reductions in public expenditure and improvements in other services which only the State can provide.

111. Would it ever be possible for all or virtually all old people to receive a pension from an occupational scheme or, in the case of the self-employed, from an approved pension plan? And would such pensions be enough, when added to a basic State pension insufficient by itself, to ensure adequate total provision for their old age?

112. During recent years the number of employees in occupational pension schemes has considerably increased: it is now over 12 million. In total the schemes have been making a major contribution to national saving. In 1967 their total income from contributions was about £1,265 million and their expenditure about £935 million. The number of people receiving occupational benefits in old age was about two million, although, as Table 4 shows, the amounts provided were often small.

### Table 4

**Amounts of pension payable to occupational pensioners, 1967 (estimated)**

<table>
<thead>
<tr>
<th>Weekly amount of pension</th>
<th>Proportion of pensioners per cent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Under £1</td>
<td>20</td>
</tr>
<tr>
<td>£1 to £2</td>
<td>20</td>
</tr>
<tr>
<td>£2 to £3</td>
<td>10</td>
</tr>
<tr>
<td>£3 to £4</td>
<td>10</td>
</tr>
<tr>
<td>£4 and over</td>
<td>40</td>
</tr>
<tr>
<td>Total</td>
<td>100</td>
</tr>
</tbody>
</table>

113. The present coverage of occupational schemes varies considerably among different groups of the population. While about 75 per cent of male non-manual employees are in a scheme, the coverage among male manual workers is probably not much more than 50 per cent. Some 75 per cent of men employed in the public sector are in occupational schemes, compared with 60 per cent of men in the private sector. The proportion of employed women who are in schemes is 25 per cent.

114. There are inherent limits to the ultimate expansion of occupational pensions. First, many of the people who have no occupational scheme work for small firms: there are about a million employers of all kinds in Britain, but less than 70,000 active pension schemes. Small employers are less equipped to have a scheme than large employers. In particular, there are many thousands of small firms—in engineering, in the distributive, building and other trades—where the employer could reasonably claim that his operation is on too small a scale, and his labour turnover too high, to justify an occupational pension scheme.
115. Secondly, the benefits of occupational schemes tend, like wages and salaries, not to be adjusted to family needs. Perhaps two-thirds of the occupational pensions at present being paid to men will die with them; and about a third of men at work today are in schemes giving no permanent widowhood pension cover once they have retired. Usually a man can make provision for his wife only by cutting into his own pension. Few wives spend sufficiently long at work to earn occupational pensions of their own.

116. It is estimated on present trends that even by the turn of the century about a third of retirement pensioner households will still have no occupational pension at all. It would be impracticable to attempt to close this gap in coverage by making occupational schemes compulsory: the control of a universal network of private schemes, even if one could be set up, would create formidable administrative and financial problems both for the Government and for the schemes themselves.

117. Finally, growth in the coverage of occupational schemes, and improvements in the levels of pensions which they award, will still leave the problem of maintaining the value of occupational pensions once they are in payment. Not all schemes have found it possible to increase pensions after retirement; and such increases as are given are often haphazard and may be inadequate. At most they do no more than compensate for rising prices. Thus, while many schemes provide pensions which are adequate at the time of retirement, there is seldom any guarantee that their value will not be eroded as time goes on. Some old people are therefore faced with the prospect of steadily diminishing resources at the same time as their capacity to improve their circumstances is also getting less.

118. It is no criticism of occupational schemes to draw attention to needs which, by their nature, they cannot be expected to meet. Their purposes are different from those of a social security scheme. They can add to the pensions of many; but they cannot be a substitute for an adequate State scheme. If adequate benefits are to be provided for the irregularly employed, the chronic sick and widows, and if additions to pensions are to be made for family responsibilities such as the care of wives who have had long periods away from employment, this is clearly a task for the State scheme and not for occupational schemes. Moreover, if there is to be a pension which is guaranteed to maintain its real value, this also is a task which the State scheme can fulfil but which raises great difficulties for occupational schemes. Occupational schemes cannot be expected to cover all needs. The Government's aim is to allow them to fulfil their essentially complementary role, as explained in the following two chapters.
PART III
CHAPTER 5
THE NEW STATE SCHEME AND OCCUPATIONAL SCHEMES

The role of occupational pension schemes

119. The new State scheme described in chapter 3 will bring considerable extra benefit cover to contributors who are members of occupational pension schemes, as well as to those who are not. Reference has already been made to the impressive growth in occupational schemes in recent years. It is estimated that at the end of 1967 there were about 65,000 active pension schemes, excluding arrangements for individuals, compared with about 37,500 in 1956. The membership of such schemes increased from about 8 million in 1956 to over 11 million in 1963 and to over 12 million in 1967. Thus half of all employed persons, including about two-thirds of all employed men, are now members of occupational pension schemes (and this takes no account of those employees who will become members of their employer's scheme as soon as they have satisfied any qualifying conditions for membership). Of the total membership, 8 million are employed in private industry and 4 million in the public sector (central and local government and the nationalised industries). The Government welcome this growth in occupational pension provision and recognise the important role which occupational schemes now play, not only in provision for old age (and to some extent for widowhood and sickness) but as a source of the savings needed to finance investment.

120. The new State scheme must provide comprehensive benefits for the population as a whole—including in particular provision for families and a guarantee that the real value of pensions will be maintained after award—which it would be difficult, if not impossible, for funded occupational schemes fully to reproduce. It would be still more difficult to rely on occupational schemes being able to match any increases in the level of State pensions in payment which went beyond maintaining their real value. But occupational schemes can be individually framed, in a way that the State scheme cannot, to meet the special requirements of particular industries and employments. They can in this way both complement and supplement the universal State provision. Membership of a good occupational scheme is commonly a highly valued feature of an employment.

121. The contribution and investment income of occupational schemes has increased over the years more than their expenditure on benefits, and there has been a steady increase in accumulated funds. Table 5 shows the estimated total income and expenditure of occupational schemes for the years 1963 and 1967, based on the results of special surveys for those years conducted by the Government Actuary(1).

TABLE 5
Finance of occupational pension schemes

<table>
<thead>
<tr>
<th></th>
<th>Contribution income (1)</th>
<th>Investment income (2)</th>
<th>Expenditure (benefits and expenses) (3)</th>
<th>Net growth of funds (4)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1963</td>
<td>850</td>
<td>325</td>
<td>615</td>
<td>560</td>
</tr>
<tr>
<td>1967</td>
<td>1,265</td>
<td>480</td>
<td>935</td>
<td>810</td>
</tr>
</tbody>
</table>

The final column of the table, indicating the difference between the total income of the funds (columns 1 and 2) and the expenditure (column 3), shows the savings made through schemes. These savings account at present for more than one-third of total personal savings and more than a tenth of total net savings.

122. The new funds accumulated in 1967 by self-administered schemes (that is, schemes other than those conducted by insurance companies) were invested as follows: 12 per cent in United Kingdom Government and local authorities securities; 59 per cent in company securities; and 29 per cent in investments of other kinds. These schemes account for about two-thirds of all occupational pension funds, from which it can be seen that the funds occupational schemes are administering play an important financial role, helping to finance investment by private industry as well as investment by public authorities and other bodies.

123. Personal savings are of economic importance because, by limiting consumption, they permit the expansion of investment needed for growth and productivity to be made without inflationary pressure. Growth in occupational pension funds has in the past made an important contribution to these savings. This growth derives from four factors: growth in membership; expansion in the scale of provision, resulting in higher contributions (as a proportion of earnings) towards more generous future benefits; the extent to which new schemes are still at the stage when funds are being built up while there is little expenditure yet on benefits; and the fact that when incomes are rising current contributions relate to higher earnings than current pensions, which are based on former earnings.

124. The growth in the number of members may have slackened recently. There is however still room for a further increase in membership, which is expected to occur particularly among women; but as coverage is now fairly wide, future growth may well be smaller than in the recent past. Contribution income is continuing to grow both because of rising earnings and because of the increasing scale of provision; and some further expansion can be expected. The effects of the recent rapid expansion will also be felt for a good many years to come. Thus it is likely that occupational pension schemes will continue for some time to provide an important source of savings.

125. In contrast to most occupational schemes, the State scheme will continue to be financed on the pay-as-you-go principle (see paragraph 43).
The contributions to it will therefore largely be used to finance current payments of benefit and will not contribute in the long run to net savings in the same sense as funded occupational schemes do while they are expanding. From the point of view of the national economy, therefore, occupational schemes and the State scheme are complementary to each other.

126. For all these reasons, there is no question of the new State provision replacing occupational schemes. On the contrary, its structure will leave ample scope for their continued development. Occupational schemes have an important part to play alongside the new State scheme, and in its widest sense national superannuation must embrace occupational as well as State pensions. As has been made clear in chapter 2, the Government’s aim is that of working in partnership. It is against this background that the need to place a ceiling on the earnings to which employees’ contributions to the State scheme are related (see paragraph 30), and the desirability of allowing some contracting out of the new scheme, have to be considered.

The present system of contracting out

127. Under the present national insurance scheme, no contracting out is allowed from either the short-term benefits or the basic flat-rate pension. The present scheme’s only contracting-out provision applies to the graduated additions to the flat-rate pension which were introduced in 1961. At that time graduated contributions applied to that part of a person’s earnings lying between £9 and £15 a week. An employer was allowed to contract out those of his employees who were qualifying under an occupational scheme for at least as much pension on retirement as they could have obtained by contributing at the maximum earnings level—£15 a week—under the State graduated scheme. Contracted-out employees and their employers paid no graduated contributions but became liable for higher flat-rate contributions than other employees and employers. If an employee who had been contracted out left his employment without being guaranteed the necessary occupational pension, his employer had to buy him back into the State scheme by paying the appropriate balance of graduated contributions.

128. The maximum level of earnings taken into account under the graduated scheme went up from £15 to £18 a week in 1963, and the amount of pension which contracted-out employees had to be guaranteed from their occupational schemes was increased correspondingly.

129. In 1966, the introduction of earnings-related short-term benefits by the present Government made it necessary to charge employer and employee an additional contribution of ½ per cent each on that part of an employee’s earnings between £9 and £30 a week. This contribution is payable whether the employee is contracted out or not; and so for the first time contracted-out employees have come within the scope of graduated liability. The basis of contracting out was not affected, since the difference in amount between the contributions paid for contracted-out employees and for other employees—and the difference between the State pensions of people in these two categories—have remained unchanged.

130. The number of employees contracted out has risen from 4½ million in 1961 to about 5½ million at present (nearly 3 million of whom are in the public service or nationalised industries).
Why the present contracting-out arrangements cannot be carried over into the new scheme

131. The present method of contracting out involves replacing the element of graduated pension, but not the basic flat-rate pension, by a pension from an occupational scheme. Irrespective of an employee’s actual earnings he must be assured by his employer, either through the occupational scheme or by an appropriate payment into the State scheme, of a pension of about 1s. 4d. a week for each year of contracted-out service, corresponding to the extra State pension obtainable by contributions over the full earnings range covered by graduated pension contributions. It follows that an employee earning less than £18 a week is guaranteed a higher pension through having been contracted out than he would have obtained under the State scheme at his particular earnings level. In the new scheme, however, the range of earnings on which the new percentage contributions will be payable is so much greater that it would be out of the question to continue to require the employer to disregard the actual earnings of the contracted-out employee and to provide even for the lowest earner a pension at the maximum level of the State scheme.

132. Any new form of contracting out must therefore require the employer to guarantee pensions for his contracted-out employees related to their actual earnings. But, even so, a system whereby contracted-out schemes had to offer a complete substitute for the State pension would be well beyond the scope of most occupational schemes. First, they would have to match the new State scheme’s weighted pension formula and twenty-year maturity—neither of which would fit easily into occupational schemes. Secondly, those schemes which do not base their pensions on final salary would have to match the regular revaluation of an employee’s past earnings record which the State scheme will provide, resulting in a steady increase in his pension rights in respect of past as well as current service; and all schemes would have to match the improvements made under the State scheme in pensions after award. In other words, whenever increases were made in the State scheme’s benefits to take account of changes in earnings standards or living costs, employers running completely contracted-out schemes would have to review their own provisions and, if necessary, make corresponding adjustments so as to ensure that their employees did not lose any improvement in pension rights granted either during service or after retirement. All this would mean that, by contracting out, an employer would be taking on commitments which were large in themselves, and of quite a different order from those which contracting out at present involves. He would also be accepting in advance additional liabilities which could not be predicted at all exactly, as they would depend upon future increases in the general level of prices and earnings.

133. A few schemes of a specialised kind might nevertheless be able to offer a benefit which was a complete substitute for the State scheme’s pension, though very complex transitional arrangements would be needed to ensure that people did not lose the benefit they had already contributed for under the present State scheme. But in the Government’s view the possibility of any such provision has to be dismissed on broader grounds. Either it would have to be the only arrangement for contracting out, in which case
the facility would be outside the compass of the great majority of occupational schemes; or there would have to be an alternative system for contracting out, more suitable for the generality of private schemes, which did not require them to match the full provision of the State scheme. A two-tier arrangement of this kind would be much too complicated. The same would be true of any proposal to extend the scope of contracting out beyond the personal retirement pension. Contracting out of the range of benefits covering sickness and unemployment would be impracticable in any event; and even if it proved practicable to extend contracting out to cover the widowhood and dependency benefits which will be financed, like pensions, from the National Superannuation Fund, this would restrict very considerably the number of schemes capable of contracting out. It would clearly lead to extensive complications if employers were offered a choice of contracting out of either all the benefits provided from the National Superannuation Fund, or the personal pension alone. This being so, the real point at issue is whether the new scheme should offer a facility for partial contracting out—that is, an arrangement whereby occupational schemes could take over responsibility for a defined part of the personal retirement pension which would otherwise be paid by the State.

*The case for partial contracting out*

134. There are arguments both for and against a system of partial contracting out. Considerations of simplicity of operation and administrative economy tell against it. And it might be argued on more general grounds that it would be acceptable for all employees to participate fully in the State scheme, with occupational schemes left free to "live on top". This is the pattern generally found abroad. In support of this approach, it could be said that occupational schemes best serve their members to the extent that they offer something additional to what can be provided under the State system; and that there would still remain ample scope for this for many employees. Within the range of earnings covered by the State scheme there is no inherent advantage for a pensioner if part of his income comes from an occupational rather than a State source.

135. The Government have however noted the strongly held view among some of those concerned with occupational pension schemes that contracting out would help to spread the burden of the growing cost of pensions more evenly over successive generations of contributors. As explained in paragraph 43, the National Superannuation Fund will be financed on the pay-as-you-go principle, which has the broad effect that contributions of each generation of contributors are used to pay for the pensions of the preceding generation. While the initial contribution rates for National Superannuation will be fixed at a level which is sufficient to finance the growing expenditure of the Fund for some years ahead, increases will thereafter be necessary. Although contributors who were contracted out of part of the State pension provision would pay total contributions comparable to those paid by those not contracted out, part of this total would not be paid to the State scheme. The immediate effect of contracting out would be to shorten the initial period during which the income of the National Superannuation Fund will exceed its outgo and therefore to require contribution rates to be increased earlier
than would otherwise be the case. But in the longer term, since lower pensions would be paid from the National Superannuation Fund to those who had been contracted out, there would be a growing offset to the loss of contribution income.

136. There is a further sense in which it is sometimes argued that contracting out would help to reduce the burden of pensions on later generations. The claim on goods and services represented by future pensions will have to be met out of future production. Apart from certain public sector schemes, occupational schemes which are contracted out need to be financed on funding principles, whereby financial provision is made during the contributor's working lifetime through the accumulation and investment of his contributions for the pension which will become payable during his old age—whereas a State scheme, financed on the pay-as-you-go principle, will not itself generate additional investment of this sort. Since contracting out would not only reduce the extent to which pension provision under the State scheme is substituted for existing occupational provision but also enable some new pension provision to be occupational rather than State, it is held that it would assist to maintain and indeed increase the flow of savings from occupational schemes. It is argued that this would be an advantageous method of increasing the funds directly channelled to productive investment and so of ensuring a bigger growth of resources which would help to reduce the burden of pensions on future generations—while at the same time the disturbance of the capital markets which might follow a large cut-back of existing occupational schemes would be avoided.

137. In any event, the new State scheme will inevitably face occupational schemes with formidable problems of adjustment. If there were no contracting-out facility, some employers and employees might be prepared to pay for both the new State pension and full occupational benefit; but the more likely reaction would be to offset the higher State contributions by reducing future payments to the occupational scheme. If this happened the scale and rate of growth of occupational schemes would be reduced and this could lead to the winding up of some of them. This in turn would involve a corresponding diminution of their contribution to savings. A contracting-out facility would limit the impact of the new State scheme on the level of occupational provision, and this would ease the situation. It would also assist the continued growth of occupational schemes and encourage employers who might otherwise have been deterred from starting new schemes to go ahead with them. Nor need administrative difficulties block the way; the present contracting-out arrangements, which have been in operation since 1961, have provided a valuable basis of experience which should enable the additional complications arising from any future system to be tackled with a reasonable measure of assurance. These considerations all lead the Government to favour the inclusion of a contracting-out facility in the new scheme.

A scheme for partial contracting out

138. Preliminary study has suggested the following as the pattern for partial contracting out. The national superannuation contribution paid by contracted-out employees, and that part of the employer's contribution on earnings up to the employees' "ceiling" (see paragraph 55), would be at a
lower percentage than would be payable for employees in general. As counterpart, there would be a deduction from the personal retirement pension which the contracted-out employee would receive under the State scheme. The occupational scheme would be required to guarantee him a pension of at least the amount deducted from his State pension. This arrangement would affect only the personal retirement pension (and not dependency or widowhood cover, which would be available in full to those contracted out) and there would be no requirement for contracted-out occupational schemes to match various special features of the State scheme, such as its weighted pension formula and twenty-year maturity. Because the occupational scheme would be assuming responsibility for only part of the personal retirement pension, and the State scheme would still be providing all its other benefits in full, contracted-out employees and their employers would of course still need to pay the major part of the normal contribution to the National Superannuation Fund. The financial implications for the National Superannuation Fund of such an arrangement are discussed by the Government Actuary in Appendix 2.

139. The formula linking the deduction from contributions to the deduction from pension would be fixed in such a way that the total amount by which contributions were reduced—for employer and employee together—represented, on average, the commercial cost of providing the pension for which the occupational scheme was taking over responsibility from the State. The main factors to be taken into account in fixing the formula would be the accumulation of interest of an invested fund, mortality, and the age distribution and earnings of contracted-out employees. With pension ages for men and women remaining at 65 and 60 respectively (see paragraph 60) there would have to be a separate formula for women, incorporating either a higher contribution reduction than for men or a smaller pension reduction. The working of the arrangements would need to be examined regularly and the formula might need to be adjusted as some of the relevant factors changed over time.

140. While a system on these lines should be technically feasible, it would raise a number of problems. The first would arise through the dynamic element in the new State scheme, since any form of contracting out must plainly leave each contracted-out employee no worse off than if he had remained fully within the State system. This would be essential because, although the employer would be required to give the employees concerned the opportunity to consider the matter beforehand, the final decision whether to contract out his occupational scheme must (as now) remain with him. On the other hand it would not be tolerable for an employee's overall pension rights to be diminished because his employer had chosen to take him out of a part of the State scheme.

141. At present there is no difficulty in ensuring that an employee cannot lose any of his personal pension rights by becoming contracted out, since he can only be contracted out of a part of the State scheme which is entirely fixed in cash terms. Achieving the same result under the new, dynamic State scheme is bound to be more difficult, as it becomes necessary to decide who should be responsible for guaranteeing a contracted-out employee those improvements in his overall entitlement which he would
have received under the State scheme. The natural answer would perhaps appear to be for this to be entirely the employer’s responsibility; but he would then have to take on an unknown commitment which would depend on future movements in price and earnings levels and, as recognised in paragraph 132, this would present very real difficulties.

142. Some difficulties may also be encountered in the settlement of terms which can be generally accepted as fair to all parties—that is, to contributors not contracted out as well as to those who are. As explained in paragraph 170, a contracting-out facility would mean an immediate loss of income to the National Superannuation Fund, as the result of which the rates of contribution payable by everyone would have to be increased earlier than would otherwise have been necessary. It would be particularly important therefore to be able to assure the generality of contributors that the contributions of the contracted out had been reduced by no more than was needed to meet the cost of providing for that part of the State pension for which the occupational scheme was assuming responsibility.

143. Further, the formula linking the contribution and pension deductions would have to be based on an estimate of future trends over a period in a number of factors, including the rate of interest. Even a small misjudgment in the initial terms could mean either that the State pensions of contracted-out employees were being provided, to some extent, at the expense of other contributors, or, conversely, that the cost of contracting out was set so high that only limited use was made of the facility, which would then no longer offer a satisfactory basis for partnership between the State and private provision. On the other hand, the contracting-out arrangements would have a better chance of working smoothly, and being generally understood and accepted as fair, if the formula were adjusted as infrequently as possible.

144. Finally, if employees are to rely on occupational schemes to provide a substantial part of the pension they would otherwise have received from the State scheme, adequate safeguards will be needed to ensure that no scheme is used for contracting out unless soundly based. In view of the increased contingent liabilities which contracting out under the new scheme would involve, it would be right to consider whether safeguards are needed beyond those which operate at present.

Public service pensions

145. Of the 12 million or so people who are members of occupational pension schemes, about 4 million are employed in the public sector and 3 million of these are contracted out of the present graduated pension scheme. They include employees of the nationalised industries, the public services (civil servants, teachers, police, firemen and the staff of local authorities and the National Health Service) and the Armed Forces. The basic provisions of many of the main public sector pensions schemes are alike: they provide for a maximum pension, at the normal retiring age, of forty eightieths of salary averaged over the last three years (one eightieth for each year of service) plus a lump sum of one hundred and twenty eightieths, or the approximately equivalent pension benefit of forty sixtieths with a right to commute up to a quarter. Arrangements have been made in successive Pensions (Increase) Acts periodically to increase pensions already being paid to retired members of the public services. Increases on a similar pattern have also been
paid to pensioners in many other parts of the public sector (including the Armed Forces) to which these Acts do not directly apply. Recently many schemes in the private sector have also found it possible to augment the pensions of their retired members, but the latest survey undertaken by the Government Actuary(1) suggests that the public sector is ahead of private sector practice in this respect.

146. As in the private sector, many public sector schemes (for example, in the nationalised industries and most of those in the public services) are contributory, but a few are non-contributory (the Civil Service and the Armed Forces) and are financed by the Government on a pay-as-you-go basis.

147. Schemes on these lines, giving relatively high pension fractions and relating pensions to earnings in the few years before retirement, are common in both the private and public sectors and will pose a problem as State pensions build up to the substantial levels to be provided in the new scheme. Some re-alignment of their terms may be necessary.

148. In the areas where the Government have an additional responsibility in their role as employer, they intend that these matters should be discussed fully with staff interests. In the Civil Service, following the recommendations on various pensions questions by the Committee under the chairmanship of Lord Fulton(2), a joint committee has already been set up to review the whole basis of superannuation, with representatives of management and staff, including the industrial trade unions concerned. The implications of the new State scheme will be taken fully into account in the course of this review. The position of the Armed Forces will also have to be considered.

Winding up of the present contracting-out arrangements and adaptation of occupational schemes

149. Because a contracting-out facility under the new scheme will have to be on a different basis from the present arrangements, rights acquired from contracted-out employment up to the start of the new scheme will need to be properly determined and safeguarded—where necessary by means of a deferred pension or an appropriate payment into the State scheme. There will, in addition, need to be statutory provision to help some occupational schemes to adapt to the new State provision, so that those responsible for them are not prevented from making necessary modifications because of legal complications.

Conclusion

150. Although the main lines of development are clear, a number of important issues remain to be settled in relation to a new system of contracting out of the State scheme. In advance of legislation, therefore, the Government intend to discuss these matters with representatives of occupational schemes and others concerned. The Government are confident that, given that all concerned are prepared to play their part in resolving the evident difficulties, fair and workable arrangements can be made for a system of partial contracting out to accompany the introduction of the new State scheme.

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(2) Report of the Committee on the Civil Service, Cmnd. 3638, 1968, paras. 136 to 139 and Appendix H.
CHAPTER 6

PRESERVATION AND TRANSFERABILITY OF OCCUPATIONAL PENSION RIGHTS

The background

151. The importance of occupational pension schemes has been referred to in chapters 2 and 5, which discussed the provision of a contracting-out facility in the new State scheme. It has been made clear that the Government attach considerable importance to the well-being of occupational schemes and see them as continuing to play a vital part alongside the State scheme.

152. The 65,000 occupational schemes vary greatly in size, scope and method of financing, and in their detailed provisions. Their variety reflects the fact that they are often individually framed to meet the needs of particular occupations or employments. But, considered collectively, they suffer from a considerable defect—there are no universal or comprehensive arrangements for safeguarding pension rights on changes of employment.

153. Ideally, when members of occupational pension schemes change jobs, they should be given the opportunity of transferring accrued rights from one pension scheme to another—thus acquiring in the new scheme benefits equivalent to those they possessed in the old. Pension rights would accumulate and move with the individual from one employment to another, finally providing a single pension on retirement.

154. While transfer arrangements between particular pension schemes do exist (and are common within the public sector) information collected by the Government Actuary's Department shows that, in practice, a transfer value in respect of their pension rights is paid for only a small proportion of those changing jobs. In 1963 only about 5 per cent of those leaving public sector employment and about 1 per cent of those leaving private sector employment had their rights transferred in this way. Rights were safeguarded by the grant of deferred pensions to 2 per cent of those leaving public sector employment and 8 per cent of those leaving private sector employment. Thus in public and private sectors together, pension rights were secured by one or other of these methods in less than 10 per cent of cases. Of the remainder—over 90 per cent—about three-quarters received a refund of their contributions to the occupational scheme, while the rest received no benefit from their membership of the scheme (other than a gratuity in a small number of cases). There is no indication that the position has changed substantially since 1963.

155. The reports published by the Government Actuary(1) make it clear that the rules of a substantial proportion of schemes do provide for the possibility of safeguarding pension rights by provision of a deferred pension or payment of a transfer value. But a majority of members who could have had their rights transferred...

(1) See footnote to para. 121.
exercised an option to take a deferred pension preferred to withdraw their contributions, while the mere possibility of paying a transfer value (which exists for 40 to 50 per cent of members of private sector schemes) does not mean that transfer arrangements between two schemes will in practice be negotiated. The difficulty of negotiating such arrangements is referred to below.

**Previous consideration of the safeguarding of pension rights**

156. The National Economic Development Council discussed this problem in 1964 and suggested that the Minister of Labour's National Joint Advisory Council (N.J.A.C.) was an appropriate forum for a full examination of all the considerations involved. The Council decided to appoint a special committee to report on the economic and social implications of existing arrangements for preservation of pension rights on change of employment, the desirability of extending such arrangements and the means of doing so. The Committee's report was published in 1966.

157. The Committee concluded that there were strong social arguments for more extensive arrangements for the safeguarding of pension rights. The extent to which the present situation discouraged mobility of labour was, they believed, limited; but it applied particularly to middle-aged employees in relatively well-paid jobs. The Committee favoured action to preserve pension rights on change of employment, by the provision of deferred pensions. They did not believe that it was feasible to require universal transferability of pension rights.

158. The Government have given very careful consideration to the report of the Committee and to all aspects of the problem. In particular they have looked at the possibility of requiring complete transferability of pension rights. The practical difficulties, many of which were set out in the Committee's report, are very great. Transferability of pension rights depends on determining the value of the rights accrued in the first scheme and establishing the rights these values represent in the second. Even when two schemes are broadly similar it may not be easy to negotiate satisfactory transfer arrangements; the number and variety of occupational pension schemes make it extremely difficult to devise rules of universal application. It would not be feasible to bring about transferability of pension rights between all schemes, either by direct legislation or by other means, except as part of a much more general control of pension schemes, which might disrupt many of them. Further, in many cases a change of job involves moving from employment covered by an occupational scheme to employment where no scheme exists. While the Government hope to see a continuing spread of transfer arrangements they have concluded that it is not at present possible to achieve universal transferability of occupational pension rights.

**Proposals**

159. The Government believe, however, that the situation must be improved. It is clearly unsatisfactory that individuals who have been members of an occupational pension scheme, perhaps for many years, should find on changing jobs that they are obliged to forfeit their pension rights.

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(1) See footnote to para. 49.
160. The new State scheme, when fully operative, will generally provide much better pensions than now. However, an employee changing jobs should, for both social and economic reasons, be able to retain the additional pension rights for which he has qualified in an occupational scheme. It is the Government's intention to bring in legislation to ensure that every member of an occupational pension scheme who has satisfied certain minimum qualifying conditions shall have the right to have his accrued pension preserved for him until he reaches retiring age.

161. However, many complex points have first to be decided. These include, how to define a method of calculating accrued pension rights which will be of universal application, and whether the preservation requirement should apply to pensions accrued before the operative date of the new legislation. On this second point, if the preservation requirement applied only to rights accruing after the operative date of the legislation it would be many years before the objects of preservation were fully met. On the other hand, the fullest consideration will need to be given to the financial burden which any retrospective requirement would impose on schemes.

162. A further point of principle concerns the right of an employee on leaving his job to withdraw the contributions which he himself has paid into an occupational pension scheme. Such a right is an almost universal feature of contributory schemes, whether or not the schemes give an employee an alternative right to have his accrued pension transferred or preserved. There are some who argue that the option to withdraw contributions should be removed and that preservation of pensions should be compulsory in all cases. In general, the report of the N.J.A.C. Committee took this view.

163. On the other hand, the right to withdraw contributions is prized by many individuals who may find a cash sum at the time of greater importance than a deferred pension. Pensions accruing under the State scheme will not be jeopardised by changes of employment and will ensure for the great majority a State pension on which they can live in retirement. In these circumstances the Government see considerable merit in leaving the individual free to decide whether to have his occupational pension preserved or to withdraw his contributions. Their view is therefore that while contributory schemes should be subject to the requirement to offer preservation arrangements, they should be allowed to provide for an employee to withdraw his contributions on leaving if he prefers. The Government would however regard it as important that a withdrawing employee should be given a clear statement of the value of the alternative options open to him.

Consultation

164. Before introducing legislation, the Government intend to discuss these matters with representatives of occupational schemes and others concerned. In view of the widespread agreement that action is needed to ensure the safeguarding of occupational pension rights they are confident that, despite the practical difficulties to be overcome, arrangements can be worked out which will represent a marked advance on the present situation.

(1) Withdrawal could not of course be permitted of any contributions paid towards that part of an occupational scheme pension which an employer had guaranteed to provide in order to contract the employee concerned out of the new State scheme.
PART IV
CHAPTER 7

THE FINANCIAL AND ECONOMIC IMPLICATIONS
OF THE NEW SCHEME

Financial implications

165. Under the existing scheme all national insurance contributions are paid into one fund and all national insurance benefits are paid out of it. Under the new scheme, as explained in paragraph 52, this single fund will be replaced by two funds, the National Superannuation Fund and the Social Insurance Fund. Each fund will receive the appropriate proportion of the total contribution income, including the Exchequer contribution. The money accumulated in the funds—including the present scheme's reserves, which will be divided between them—will bring in interest which will, as now, help towards meeting the scheme's expenditure.

166. As shown in Table 6 in the Memorandum by the Government Actuary on the finance of the proposals (Appendix 2) the cost of the scheme will grow as the full rates of pension come gradually into payment over the first twenty years, and as the proportion of pensioners receiving the full rates increases.

167. In principle the new scheme, like the present one, will be financed on a "pay-as-you-go" basis—that is, with current income designed to meet current expenditure. Most people must expect, however, to pay more for their higher benefit prospects. Furthermore, frequent changes in the percentage contribution rates ought to be avoided, especially in the early years when the scheme is settling down. The initial national superannuation contribution rates proposed (see paragraphs 56 and 58) leave room, therefore, for the growth of expenditure for some years ahead.

168. The result is that there will be a surplus of income over outgo in the National Superannuation Fund at the outset of the new scheme. How long this position will last depends upon the actual levels of income and outgo; and these in turn depend on a number of factors. Most important among these are: the extent to which, over the years, the growing national income will permit improvements in the real value of pensions after award; the arrangements for contracting out; and the number of employees covered by these arrangements.

169. The two-yearly reviews of pensions in payment (see paragraph 101) will ensure that, as a minimum, they are raised sufficiently to compensate for any rise in prices. The costings of the new scheme have been done in terms of April 1968 earnings levels. They therefore illustrate what the relative growths of income and expenditure would be if pensions in payment were always to rise in line with earnings. However, the figures do not take
account of contracting out. Because decisions have still to be taken on the
degree of contracting out in the scheme, the Government Actuary has given
estimates of what the position would be if there were no contracting out at all,
accompanied by an indication of the effect of each $\frac{1}{2}$ per cent a side by which
the contribution was reduced for those contracted out. (See Appendix 2,
paragraph 14.)

170. The Government Actuary estimates that with contributions at the
proposed level, and before making any allowance for contracting out, the
accumulated National Superannuation Fund would reach a maximum of about
£3,400 million (in addition to its share of the present reserves) in 1987–88,
the year in which expenditure would exceed income for the first time.
The contribution rates would then need to be increased somewhat, to
maintain income in line with expenditure, on the pay-as-you-go principle.
If the numbers contracted out were the same as at present, the point at which
expenditure first exceeded income would be advanced by about 18 months
for every $\frac{1}{2}$ per cent a side by which the contribution was reduced for those
contracted out, and the maximum size of the fund would be correspondingly
reduced.

171. Against the expenditure on pensions there will be some saving
because of the gradual reduction in the number and amounts of supplementary
benefits in payment to pensioners. It is not possible to provide any accurate
forecast of these savings. Expenditure on supplementary benefits is at present
about £450 million a year (of which over £200 million is for pensioners). The
prospect is that, in terms of 1968 levels, this will decline after the start of the
new scheme, though only slowly during the first decade or so, with the
probability that by the turn of the century expenditure or supplementary
benefits will be at a very much lower level.

Economic implications

172. The main purpose of the new scheme is to raise the standard of
living of pensioners, both absolutely and in relation to the rest of the
population. It is estimated that at present national insurance and supple­
mental benefits provide pensioners with about a third of the average income
of the rest of the population(1). Other sources provide about a further third,
so that the average income of pensioners is now around two-thirds of that of
the rest of the population; but there are wide variations on either side of
these average levels.

173. When the new scheme has been running long enough for the bulk of
pensioners to be receiving pensions at the fully mature new rates—that is,
some time after the turn of the century—the pensions provided might amount
on average to nearly half the average income of the rest of the population.
This would mean that, even if the relative provision from other sources were
no greater than now, the average income of pensioners would approach
80 per cent of that of the working population.

174. The improvement in the relative standard of living of pensioners will
not be spread evenly throughout the retired population, but will tend to be
concentrated on the groups with fewest resources beyond their State retire­

(1) In estimating average income per person, children are counted as a half.
ment pension. Those who will gain most will be the widows, who often have no appreciable other income of their own.

175. At present, pensioners account for 10 per cent of total personal consumption, and the rest of the population for 90 per cent. The projected increase in the living standards of pensioners might raise their share of personal consumption to about 12 per cent by the turn of the century, thus reducing the share available to the rest of the population by about 2 per cent of the total.

176. The reduction in the share of personal consumption going to the working population represents the real burden of the new pension scheme. From the point of view of each contributor, the scheme implies some postponement of consumption from the working years to the years of retirement. For the community as a whole, what is available for personal consumption at any one time is determined by the potential size of the total national product and by the claims of investment, public services and exports. As long as the scheme does not result in an increase in the total proportion of the national income devoted to personal consumption, there should be no adverse effect on productivity or employment, or on future economic growth.

177. The extra burden on the working population which the new scheme involves will come about gradually over a period of 30 years or more, during which living standards can be expected to rise by at least 2 per cent a year on average, or by a total of some 80 per cent over 30 years. If they do so rise, the introduction of the new scheme might mean that workers' living standards would increase by 77 per cent rather than 80 per cent. In other words, at any rate of economic growth comparable with what has been achieved in recent years, the increase in pensioners' living standards should not be felt by the working population as an appreciable burden.

178. As explained in paragraph 167, the Government have decided that at the start of the scheme the level of contributions should be somewhat higher than is necessary to meet the expected current expenditure. The resulting surplus in the scheme's early years will have a restraining effect on the pressure of demand, and thereby enable any given level of public expenditure to be financed with a somewhat smaller recourse to general taxation. The extent of this easement will depend on how far the surplus is offset by any consequential reduction in private savings as a whole, including savings through occupational pension schemes. It would be prudent to assume, at any rate initially, that there will be some effect on occupational pension schemes which will not be fully offset by increases in other forms of private saving.

179. It is estimated that the increase in employers' contributions to 6½ per cent of earnings (including their contributions to the Redundancy Fund) implies an increase of about ½ per cent in total labour costs, which in turn —taking both direct and indirect effects into account—may increase the general level of prices by a similar percentage. There may thus be a small adverse impact on the balance of payments when the new scheme begins.

Conclusion

180. The new scheme requires people to spread their incomes more evenly throughout their lives, so that they have somewhat less during working life and substantially more during retirement. From the social point of view,
it implies a long-term commitment, by the Government on behalf of the community as a whole, to reduce substantially the present gap between the living standards of the working population and the retired population. This change will come about gradually; and it will still leave the working population able to look forward to a steady improvement in their living standards.
APPENDIX 1
FURTHER NOTES ON THE NEW SCHEME

1. This Appendix contains further notes on the following aspects of the new scheme—
   (1) The assessment of employees’ contributions.
   (2) Administrative consequences of the new earnings-related contributions.
   (3) The assessment of employers’ contributions.
   (4) Pension ages.
   (5) The retirement condition and earnings rule.
   (6) The transition from present-scheme pensions to new-scheme pensions.
   (7) Credited earnings.
   (8) Pension provision for married women.
   (9) The practical difficulties of applying earnings-relation to the self-employed.
   (10) Contribution arrangements for low earners and non-earners.

2. Except where otherwise stated, all paragraph references are to the main text of the White Paper.

   (1) The assessment of employees’ contributions
      (See paragraph 54)

   3. The present graduated contributions are assessed on the amount of pay received by the employee in each week (or other pay period) taken by itself. This means that employees whose pay is sometimes above and sometimes below the scheme’s earnings ceiling may pay substantially less in contributions, and qualify in consequence for lower pensions, than others with the same total earnings spread more evenly over the year.

   4. The new scheme’s method of assessment will avoid this unfairness. The employee will contribute on the whole of his earnings in the employment in each tax year, as he receives them, up to the annual earnings ceiling. The 7 per cent or so of employees whose earnings reach the ceiling in any year will then pay no further contributions until the following tax year. This method of assessment will ensure that the total amount of the employee’s earnings which ought to count for benefit is always matched by the amount of his contributions. It will also be simpler than the present system, which necessarily applies different ceilings to, for example, a week’s, a fortnight’s and a month’s pay.

   (2) Administrative consequences of the new earnings-related contributions
      (See paragraph 54)

   5. The replacement of the present dual system of flat-rate and graduated contributions by the new earnings-related contributions should produce a considerable net saving in employers’ administrative costs. As with the present graduated contributions, the employer will record the contributions on his employees’ PAYE documents and will remit the amounts to the Collector of Taxes. Employers will no longer need to be concerned with national insurance stamps and cards.

   6. Net savings can also be expected in the administrative costs incurred by the Government in collecting and recording contributions. A new computer complex at the Newcastle Central Office of the Department of Health and Social Security will keep contributors’ records and calculate their pensions. This will supersede the clerical methods of recording used for the present flat-rate contributions.

52.
7. At present the regular statistics of numbers in employment are based on the number of national insurance cards exchanged by employers each quarter. When the national insurance cards are withdrawn a new method of compiling employment statistics, probably by means of a simple return from all employers, will be introduced. Tests on the most suitable methods will be carried out in the next two years.

(3) The assessment of employers' contributions
(See paragraph 58)

8. The absence of an earnings ceiling for employers' contributions means that their liability will be assessed on the total pay of their employees, as recorded for PAYE. This is both fair and straightforward for employers to operate.

9. It might be suggested that employers' contribution liability ought to be tied still more closely to that of their employees, by being assessed only on the amount of each employee's earnings up to the employees' earnings ceiling—just as the present graduated scheme's ceiling applies to employers' as well as employees' contributions. In the new scheme, however, with contributions assessed on an annual basis (see paragraph 4 of this Appendix), an earnings ceiling for employers' contributions is not only unnecessary but would have undesirable effects. There would, for instance, be no satisfactory way of apportioning contribution liability between employers (whether by refund or otherwise) in cases where an employee whose total earnings in the year exceeded the annual ceiling had received those earnings in more than one employment—whether because he had changed jobs in the course of the year or because he worked regularly for more than one employer. In practice the employees' contributions in such cases could not be adjusted by reference to the employee's earnings ceiling without making one employer's liability depend on what the employee had earned with another employer. With no earnings ceiling for employers' contributions, difficulties of this kind will not arise. Each employer will contribute solely according to his own payroll: his liability will be unaffected by any earnings which his employees may have in other employments.

10. The effect of having no earnings ceiling for employers' contributions has been taken into account in deciding their percentage contribution rate under the new scheme. As indicated in paragraph 58, an estimated 1\% per cent contribution is needed from employers for the Redundancy Fund. Had their total percentage rate (without an earnings ceiling) for the remaining purposes been made the same as that paid by employees (with a ceiling), employers as a whole would have paid, at April 1968 earnings levels, about £80 million a year more for these purposes than employees. The contribution rates actually proposed will reduce this margin to about £30 million a year.

(4) Pension ages
(See paragraph 60)

Men's pension age

11. Although some occupational schemes provide pensions before age 65, there are strong reasons against lowering the present men's pension age of 65 in the State scheme. Such a move would undoubtedly encourage earlier retirement, when the general need of the country's economy is for people to continue in work as long as possible; and the increase in pension expenditure and loss of contribution income would be serious.

12. On the other hand, the Government do not consider that men's pension age should be raised above 65. This would take away, without good reason, the long-established right of a man to obtain at that age the pension for which he has contributed over many years. The right way to deal with the question of men retiring later than age 65 is to provide higher pensions for those who do so; and under the new scheme this will be done as indicated in paragraph 60. Pension age for men will therefore remain at 65.
13. On the grounds of strict equity, it can be argued that women's pension age should be brought into line with that of men, by raising it to 65. But a social security scheme must take into account the normal family situation. Most men reaching age 65 are married, and on average their wives are about three years younger than they are. Equality of pension age would therefore usually mean that, when a husband reached pension age and retired, it would be some time, often several years, before the wife could draw any pension she herself had earned. This delay would occur even if she had ceased employment and was for all practical purposes retired like her husband.

14. Nor would raising women's pension age to 65 produce a large immediate saving in benefit expenditure. As described in paragraphs 72 to 85, the new scheme, like the present one, must include provision for wives and widows on their husbands' records; the immediate saving would therefore be made primarily on the pensions of single women. At present they form about 12 per cent of women reaching age 60; but the proportion is steadily declining and by the end of the century is expected to fall to only about 5 per cent. Moreover, a move from age 60 to 65 would have to be phased gradually over a number of years in order to avoid hardship and unfairness; and this would reduce the saving still further.

15. The Government therefore do not consider that there is a sufficient case for raising women's pension age. Leaving it at 60 will normally ensure that, when husband and wife effectively become a retired couple, both will be able to draw whatever pension they have earned.

(5) The retirement condition and earnings rule

(See paragraph 60)

16. Since 1946, following a recommendation in the Beveridge Report(1), the national insurance pension has been, not an old age pension, but a retirement pension: that is, during the first five years after pension age its award is conditional on retirement from regular employment. People who defer their retirement beyond pension age can qualify for higher pensions when they eventually retire.

17. The essential purpose of pensions is to replace normal earnings when these cease at the end of working life; and the retirement condition accordingly prevents pensions being paid, on top of earnings, to people who do not retire on reaching pension age. Enforcement of the retirement condition obviously requires some means of preventing a person from obtaining a pension by declaring his retirement and then drawing it in full however much work he does. This is the function of the earnings rule, under which, up to age 70 (men) or 65 (women), retirement pension is subject to reduction if the pensioner earns more than a certain amount. This amount is at present £6 10s. a week; for the first £2 a week of earnings beyond this the reduction in pension is 6d. for each 1s. of earnings, and thereafter 1s. for each 1s. The earnings rule does no more than adjust the amount of pension payable, according to the pensioner's earnings. No limit is placed on the amount of work pensioners may do; and if a pensioner returns to regular work he can, if he prefers, cancel his retirement and so earn a higher eventual pension. At present, of about 14 million(2) retirement pensioners to whom the earnings rule applies, about 20,000 are having their pensions reduced or extinguished because they are earning more than £6 10s. a week. At age 70 (men) or 65 (women) both the retirement condition and the earnings rule cease to apply.

18. So long as a retirement condition remains, something corresponding to the present earnings rule is needed to support it; the two stand or fall together. To abolish them would increase the scheme's expenditure by about £150 million a year initially at April 1968 levels; and most of this would be spent in supplementing the earnings of some 350,000 people who were still in regular

(1) Cmd. 6404, paras. 133 to 136 and 244–5.

(2) Counting a married couple as one pensioner, where the wife has a pension on her husband's insurance.
employment. It is difficult to predict the effect of this on the pattern of work among people over pension age; but it might well produce a net decrease rather than an increase of employment. Some pensioners would be encouraged to earn more, where circumstances permitted; but they would be likely to constitute only a very small proportion of the total, judging from the fact that the vast majority of present pensioners who could be affected by the earnings rule are either not working or else have earnings substantially below the point at which the earnings rule begins to apply(1). Increases in employment among some pensioners could be more than offset by a reduction of working hours among the 350,000 people still in regular employment, who would find themselves with pensions as well as earnings.

19. Taking into account the economic, financial and social considerations involved, the Government have concluded that, as at present, the State scheme should not provide people in regular employment with pensions merely because they have reached the minimum age at which pension can be paid. Something like the existing retirement condition and earnings rule will accordingly remain.

(6) The transition from present-scheme pensions to new-scheme pensions
(See paragraph 61)

Pensions for people reaching pension age during the first twenty years of the new scheme

20. As explained in paragraph 61, the pensions for people who reach pension age during the new scheme’s twenty-year maturity period will be based on their records under both the present flat-rate scheme (the “old scheme”) and the new scheme. Their pensions will be at rates intermediate between the old-scheme rate and the fully mature new-scheme rate. The “old-scheme rate” used in the calculation will be based on the rate currently in payment to old-scheme pensioners at the time when the person concerned reaches pension age. The “new-scheme rate” used in the calculation will be the rate obtained by applying the new scheme’s pension formula to the contributor’s average earnings since the new scheme began (each year’s earnings being re-valued as in paragraph 68). After award the total pension calculated in this way will be reviewed every two years as described in paragraphs 100 to 103. Any pension earned by contributions to the present graduated scheme will be paid in addition.

21. The following examples illustrate how the calculations for a single person will be made. There will be corresponding calculations for a married couple—see paragraph 74. For simplicity, the examples are based on April 1968 levels, both for the old-scheme pension rate (£4 10s. standard rate for a single person) and for national average earnings (£22 a week). The corresponding cash amounts in the future will depend on the increases in these two levels which have taken place meanwhile.

Example 1: A person reaches pension age after the new scheme has been running for five years. His yearly contribution average under the old scheme is 50 or more, corresponding to full old-scheme pension (£4 10s. a week). His average earnings under the new scheme are the same as the national average of £22 a week; this average would correspond to a new-scheme pension, at full maturity, of £9 7s. a week (see column (3) of Table 3 in paragraph 71). His pension is therefore—

\[
\left(\frac{50}{50} \times £4\ 10s.\right) + \left(\frac{7}{50} \times £9\ 7s.\right)
\]

= £5 14s. a week.

This is a quarter of the way between the old-scheme rate of £4 10s. and the fully mature new-scheme rate of £9 7s.

(1) See the Report of the National Insurance Advisory Committee on the Question of the Earnings Limit for Retirement Pensions (Cmnd. 3197, 1967, paras. 16 to 28 and Appendices II and III).
Example 2: A person with the same old-scheme and new-scheme averages as in example 1 reaches pension age after the new scheme has been running for ten years, i.e. half-way through the maturity period. His pension is therefore—

\[(\frac{1}{8} \times £4\ 10s.) + (\frac{1}{8} \times £9\ 7s.)\]

= £6 19s. a week.

This is half way between the old-scheme rate and the fully mature new-scheme rate.

Example 3: A person reaches pension age after the new scheme has been running for fifteen years. His yearly contribution average under the old scheme is 45, corresponding to old-scheme pension of £4 a week. His average earnings under the new scheme are 1\frac{1}{4} times the national average—that is, £27 10s. a week; this average would correspond to a new-scheme pension, at full maturity, of £10 15s. a week (see column (3) of Table 3 in paragraph 71). His pension is therefore—

\[(\frac{1}{8} \times £4) + (\frac{1}{8} \times £10\ 15s.)\]

= £9 1s. a week.

This is three-quarters of the way between the old-scheme rate and the fully mature new-scheme rate.

Pensions for people reaching pension age after the first twenty years of the new scheme

22. The pensions for people who reach pension age after the new scheme's twenty-year maturity period will be based simply on their average earnings since the start of the scheme: that is, they will be entitled to the full new-scheme rates produced by the pension formula, without regard to their record under the old scheme.

Fall-back rule for certain cases

23. For a few people with no or a very low new-scheme record, the phasing out of the old-scheme record over twenty years could result in a smaller pension than they would have received had the old scheme continued. A fall-back rule will be included to prevent a reduction of pension rights in these circumstances.

(7) Credited earnings

(See paragraphs 69, 75, 87 and 89)

24. Credited earnings, normally at half the national average, will count for both long-term and short-term benefits as appropriate.

25. Where the contributor's relevant earnings record is less than half the national average, the amount of earnings credited will be limited correspondingly. Without such a limitation, those low earners who remained on benefit would become entitled, even though paying no contributions, to higher rates of benefit in the future than others with a similar level of earnings who worked and paid contributions.

26. At the other end of the scale, credited earnings will not be allowed to bring a contributor's record for any year above the ordinary earnings ceiling.

(8) Pension provision for married women

(See paragraph 72)

27. For the reasons explained in paragraph 39, the new scheme will still provide many married women and widows with pensions based on their husbands' records. The Government have examined the alternative possibility of crediting them with earnings for periods in which family responsibilities prevented them from going out to work, so enabling them to build up adequate records of their own. But special credits of this kind would produce serious difficulties, for the following reasons:

(1) There could be no real justification for crediting a housewife with earnings unless her circumstances were such as to make it unreasonable
to expect her to go out to work—because she had children at home or, for example, was looking after a sick husband. Reliance on credits restricted in this way would, however, often mean lower pension entitlement for a wife than is given by the present right to a pension on her husband's record. It would also involve making very difficult judgments in individual cases about whether a wife had good reasons, of the kinds laid down, for not going out to work. This would create an immense new burden of claims, decisions, appeals and record-keeping.

(2) If earnings were credited to married women at a level sufficient to provide enough pension for those who, through widowhood or some other cause, were left to fend for themselves, the credit level would necessarily be over-generous for the ordinary case of a wife living with her husband. There could not therefore be one uniform level of credits which could be merged with the wife's earnings in other periods in order to provide her with a single independent record. The credits would have to be worth different amounts according to the wife's domestic circumstances at the time her pension or other benefit was paid—a complication hard for those concerned to understand, under an arrangement purporting to provide married women with independent records of their own.

28. The Government have concluded that there is no satisfactory way in which housewives could be credited during marriage with earnings they have not in fact received, in order to help them acquire pensions independently of their husbands' records. Pensions will therefore continue to be available for married women and widows on their husbands' insurance, as described in paragraphs 72 to 85.

(9) The practical difficulties of applying earnings-relation to the self-employed
(See paragraphs 97 and 98)

29. At present about 1¾ million people come within the self-employed category for national insurance. They include a very wide variety of men and women working on their own account, among them people in the various professions, shopkeepers, farmers and others running their own businesses, both large and small. In general they are assessable for income tax under Schedule D and do not come under the PAYE system(1). They are not covered by the present graduated scheme and therefore pay only flat-rate contributions. Apart from unemployment benefit and industrial injuries benefits, their range of benefit cover is the same as for employees.

30. There are great practical difficulties in relating the contributions and benefits of self-employed people to their earnings. These difficulties would exist whether their contributions were to be calculated on all their earnings up to the ceiling (as is proposed for employees) or, as a supplement to basic flat-rate contributions, only on that part of their earnings which lay above a certain level. An assessment of earnings would be required for many cases where, since there is clearly no liability for tax (for example, because of the size of the total personal tax allowances due), no assessment at all is made at present. In many other cases where only a small amount of tax is at issue, much more detailed enquiries would have to be made than are required now. There is the further problem that to charge earnings-related contributions on the unadjusted figure of profits as assessed for tax under Schedule D would lead to serious anomalies in many cases. This is because the Schedule D figure may be affected by factors which ought to play no part in the calculation of contribution liability and benefit entitlement: examples are the tax adjustments arising from the way in which a taxpayer has chosen to claim relief for a trading loss, or from the incidence of capital allowances. Additional complications would arise because Schedule D tax is in general assessed not

(1) Among the minority who do come under the PAYE system, it may be possible to bring some into the employed category under the new scheme, so bringing the two systems closer into line. This is being studied.
on the current year's income, to which PAYE applies, but on the income of the preceding year. Thus if earnings-related contributions for self-employed people were to be linked to the rules which have been found necessary for Schedule D tax assessment, an intricate series of adjustments to the figure of trading profits as determined for income tax would often need to be made before it would provide a reasonable basis for calculating their contributions and benefits.

31. All this extra work would not only increase the strain on the heavily burdened accountancy profession; it would also require an estimated 2,000 or so additional Government staff. A large proportion of these would need to be Inspectors of Taxes, a grade which it is difficult to maintain at the numbers already required. The amounts of contribution which would result from all this extra effort would often be small. The extra manpower needed would be still greater if a special new system, outside the tax arrangements, were to be set up for assessing and collecting earnings-related contributions from the self-employed.

32. These difficulties rule out earnings-relation for the self-employed, at any rate for the time being. Self-employed people will therefore continue to pay contributions at a flat rate. This does not mean that they will be in a separate scheme. As explained in paragraph 98, their contributions will be counted as equivalent to earnings-related contributions on earnings of half the national average, and will be entered in the same records as the contributions for employees.

(10) Contributions arrangements for low earners and non-earners
(See paragraph 99)

33. Where an employee falls outside the scope of the PAYE system, this is nearly always because his earnings are below the minimum figure to which PAYE applies—at present £5 5s. a week for main employments. Something like 1½ million people are thought to be in this category at present. Of these, probably more than half are married women who have chosen not to pay the flat-rate national insurance contribution; many of the others are juveniles and pensioners. Earnings-related contributions on earnings which are too low to come within PAYE would amount to only a few shillings a week, yielding correspondingly small amounts of benefit. The collection of such contributions, whether done by extending the PAYE system or through some separate machinery, would often be difficult and disproportionately costly. It is therefore proposed that those whose earnings are too low to come within PAYE should not be treated as employed persons under the new scheme. Some of those who have more than one such small job will qualify to be treated as self-employed. The others will count as non-employed and so be able to contribute voluntarily as described in paragraphs 36 and 37 of this Appendix. All will still be able to qualify, where appropriate, for benefit under the industrial injuries scheme (entitlement to which does not depend on the employee's contribution record).

"Class 3" contributions

34. Contributions as a non-employed person—"class 3" contributions—are paid at present by about a quarter of a million people at any one time, in very varied circumstances. Some class 3 contributions cover no more than a week or two between jobs, or a period of unpaid holiday. Others are paid over a prolonged period by, for example, women at home looking after their parents, or housewives who, though no longer going out to work, wish to keep up their contribution record so as to qualify for a pension in their own right at age 60. In general class 3 contributions count for all national insurance benefits except unemployment benefit, sickness benefit and maternity allowance. In April 1968 the total class 3 contribution rates were 16s. 7d. a week for men and 12s. 11d. for women.
35. People without earnings are not easy to fit in as contributors under an earnings-related scheme. But it would be wrong to abolish class 3 contributions altogether. This would deprive many present contributors of the right, which they have been exercising for years, to keep up their record for pensions and other benefits at the full standard rates provided by the present scheme. Further, under the new scheme some people will have only a low record from their earnings in a particular year, either because their earnings level is itself low or because they are off work for part of the year in circumstances which do not qualify them to have earnings credited—for example, on unpaid holiday. They too need to be able to pay class 3 contributions to prevent an undue reduction in their pension expectation.

36. Class 3 contributions will therefore continue under the new scheme, to enable a contributor's record for any year to be brought up to a certain level (but no higher). This level will be set and maintained so as to correspond, at any given time, to new-scheme pension entitlement at whatever is then the standard rate in force for present-scheme pensioners. The range of benefit cover will remain as described in paragraph 34 of this Appendix. In this way entitlement to existing rights will be preserved.

37. Payment of the present class 3 contributions is compulsory in some circumstances and voluntary in others. The new-scheme class 3 contributions will be voluntary in all cases, since the amount needed to bring a person's ordinary record in any year up to the class 3 level will not usually be known until after the end of that year, and the full amount involved would often then be too large for a person with little or no earnings to be required to pay. People will be able to pay either the full year's amount or a lesser amount; and an adequate period will be allowed for payment. Facilities will also be provided, through stamped cards or otherwise, for regular payment throughout the year by those whose circumstances are sufficiently stable to enable them to foresee how much they will want to pay within the permitted range.
APPENDIX 2

MEMORANDUM BY THE GOVERNMENT ACTUARY ON THE FINANCE OF THE PROPOSALS

1. The cost of the present national insurance scheme is met by contributions from insured persons, employers and the Exchequer, the aim being to ensure, as nearly as practicable, a balance between income and outgo. The existing funds are merely a reserve—at present about 60 per cent of the annual outgo—the interest on which makes a small contribution towards the cost of benefits. The proposed scheme will be financed in the long term on the same principles, although the initial contribution will allow for the growth of expenditure over a number of years ahead and will lead to a moderate surplus in the early years.

Basis of the estimates

2. In a period of rising earnings, estimates of income and outgo expressed in monetary terms would need to be compared with estimates of national income; all such estimates would involve speculative assumptions regarding future rates of increase of prices and earnings. Contribution income in an earnings-related scheme will rise automatically with earnings and, under the proposals, newly awarded pensions will also reflect rising earnings. It is also intended that, after award, the real value of pensions will at least be maintained when prices rise. Estimates based on constant earnings give a realistic indication of the relative progress of income and outgo if benefits as well as contributions were to rise in line with earnings and, following the practice adopted in recent years in reports on the national insurance scheme, this basis has been used for the present memorandum.

3. The estimates are based on the level of earnings in April 1968 (when national average earnings were about £22 a week)\(^{(1)}\). In order that the new earnings related benefits and the flat-rate benefits of the present scheme should be on a comparable basis, the latter have been taken at 3\(\frac{1}{2}\) per cent above the current rates, which came into operation in October 1967, to allow for changes in prices and earnings between that date and April 1968.

4. The major costs in the early years of the new scheme will arise from pensions awarded wholly or partly under the provisions of the present scheme, and the conditions under which benefits will be granted will be generally similar to those applying at present. Rates of claim and other factors have, therefore, been derived from recent experience of the present scheme. On Government instructions an unemployment rate of 2 per cent has been assumed.

5. The scheme to which the present estimates relate is described in detail in chapter 3 and Appendix 1. It is proposed that the initial total contribution rate should be 6\(\frac{1}{2}\) per cent of earnings, subject to a ceiling of about 1\(\frac{1}{2}\) times national average earnings (£1,700 a year at April 1968 levels) for employees, with the same percentage from employers calculated on the employees’ earnings without a ceiling. These rates would cover national superannuation and social insurance benefits, industrial injuries benefits, a contribution towards the cost of the National Health Service and the employer’s contribution to the Redundancy Fund. Appropriate rates of contribution related to the benefits covered will be paid by self-employed and voluntary contributors. The contributions for the new scheme will be augmented by Exchequer supplements representing about the same proportion of the total contributions of insured persons and employers as at present.

6. Under the new scheme there will be two separate funds, the National Superannuation Fund covering retirement pensions, widows’ benefits and death grant and the Social Insurance Fund covering the other benefits including

\(^{(1)}\) See footnote \(^{(2)}\) on page 20.
the proposed new attendance allowance. Specific rates of contribution will be fixed for the two funds, and the present scheme’s reserves will be apportioned between them when the new scheme comes into operation.

7. As indicated in paragraphs 56 and 58, the National Superannuation Fund will initially receive contributions of 4\% per cent of earnings, subject to a ceiling, from employees, and 4\% per cent of earnings without a ceiling from employers. A contribution of 1\% per cent of earnings from employers has been allowed for the Redundancy Fund, and 2 per cent a side for the Social Insurance Fund, industrial injuries benefits and the National Health Service.

Social Insurance Fund

8. In the Social Insurance Fund, long-term sickness benefit will be earnings-related and based on the same formula as retirement pensions. The precise details of short-term sickness, unemployment and maternity benefits have not yet been settled, but it is proposed that married women should be entitled to the full personal rates of sickness and unemployment benefit instead of the reduced rates paid at present, and that employed married women within the scope of PAYE should no longer be able to choose not to contribute and should thus become eligible for all benefits. It is estimated that, allowing for these changes, a contribution of 2 per cent of earnings a side, subject to the ceiling for the employee, would be sufficient to maintain a balance of income and outgo in the Social Insurance Fund if short-term benefits are on about the same scale as now and would provide contributions for industrial injuries benefits and the National Health Service at about the same level in relation to earnings as at present.

9. On the assumption of stable claim rates, the contributions required for the Social Insurance Fund would remain almost constant for a long period. This fund will be particularly susceptible, however, to short-term fluctuations due to such factors as sickness epidemics or changes in the level of employment and will need to retain an adequate working balance to meet such contingencies.

National Superannuation Fund

10. The National Superannuation Fund will cover retirement pensions, widows’ benefits and death grant; the full earnings-related pensions awarded after 20 years will be based on a formula giving 60 per cent of average earnings up to half national average earnings (about £11 a week at April 1968 levels) and 25 per cent of higher earnings up to a ceiling of one and half times national average earnings (about £33 a week, or £1,700 a year, at April 1968 levels). Estimates of the cost of these benefits on the basis of constant earnings, and assuming that the new scheme will come into force in April 1972, are shown in Table 6, together with corresponding figures for the benefits of the present scheme if it were to continue unchanged.
TABLE 6
Estimated cost of benefits of the National Superannuation Fund (calculated at April 1968 earnings levels(184,453),(838,706)
£ million

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
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<tr>
<td>Retirement pensions</td>
<td></td>
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<tr>
<td>Present scheme</td>
<td>1,712</td>
<td>1,854</td>
<td>1,954</td>
<td>2,049</td>
<td>2,132</td>
<td>2,196</td>
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<td>Extra cost</td>
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<td>181</td>
<td>386</td>
<td>628</td>
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<td>Proposed scheme</td>
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<td>2,760</td>
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<td>144</td>
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<td>Extra cost</td>
<td>11</td>
<td>15</td>
<td>25</td>
<td>35</td>
<td>49</td>
<td>60</td>
<td>67</td>
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<tr>
<td>Proposed scheme</td>
<td>169</td>
<td>166</td>
<td>169</td>
<td>173</td>
<td>179</td>
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<td>Death grant</td>
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<td>15</td>
<td>17</td>
<td>19</td>
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<td>Total cost of National Superannuation Fund benefits</td>
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<td>Present scheme</td>
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<td>2,020</td>
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<td>2,206</td>
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<td>2,343</td>
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<td>Extra cost</td>
<td>16</td>
<td>73</td>
<td>206</td>
<td>421</td>
<td>677</td>
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<td>Proposed scheme</td>
<td>1,898</td>
<td>2,093</td>
<td>2,321</td>
<td>2,627</td>
<td>2,958</td>
<td>3,300</td>
<td>3,574</td>
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Notes
(i) These figures represent costs to the National Superannuation Fund and do not take account of any consequential savings in supplementary benefits (see para. 171).
(ii) No allowance is made for any reduction in expenditure on pensions resulting from contracting out of the new scheme (see para. 12 below).

11. The rising extra cost shown in the table compared with the present benefits reflects the gradual increase in the average pensions awarded during the twenty-year maturity period and the growing proportion of pensioners in receipt of new scheme pensions. The extra cost of widows' benefits includes the cost of paying scaled-down widows' pensions to certain widows whose husbands have died before the start of the new scheme (see paragraph 81 of the White Paper).

12. It is the Government's intention to enter into discussions with interested parties with the object of devising a system of partial contracting out for members of occupational pension schemes (see chapter 5). It is envisaged that both the persons covered by such arrangements and their employers will pay lower contributions than those for the generality of employees and that there will be corresponding deductions from personal retirement pensions. This will have a material effect on the finances of the scheme, since the reduction in contributions will be felt immediately, but the corresponding saving in expenditure on pensions will emerge only gradually as the individuals concerned come to draw their pensions. Until the terms of contracting out have been fixed and details become available about the numbers involved it is not possible to estimate what its effect will be. The estimates shown in the tables make no allowance for contracting out but, in paragraphs 14 and 17 below, some indication is given of the possible effect on the fund.

The progress of the fund

13. Table 7 shows how the income from contributions of 4½ per cent of earnings, subject to a ceiling, from employees and 4½ per cent of all earnings from employers, together with Exchequer supplements and interest, would exceed outgo in the early years. The figures, like those in Table 6, are based on constant earnings. They indicate that, subject to the qualifications set out in the following paragraphs, and before allowing for contracting out, the income, including interest on the growing fund, would exceed outgo for about 15 years.
### TABLE 7
Estimated income and outgo and changes in the balance in the National Superannuation Fund on the basis of the proposed initial rates of contribution

*(Based on April 1968 earnings and with no allowance for contracting out)*

<table>
<thead>
<tr>
<th>Year</th>
<th>Expenditure on benefits</th>
<th>Costs of administration</th>
<th>Contributions from insured persons and employers</th>
<th>Exchequer supplements</th>
<th>Interest*</th>
<th>Excess of income over outgo</th>
<th>Balance at beginning of year†</th>
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<tr>
<td>1972-73</td>
<td>1,898</td>
<td>37</td>
<td>1,941</td>
<td>361</td>
<td>31</td>
<td>398</td>
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<tr>
<td>1977-78</td>
<td>2,093</td>
<td>40</td>
<td>1,969</td>
<td>366</td>
<td>81</td>
<td>283</td>
<td>1,756</td>
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<tr>
<td>1982-83</td>
<td>2,321</td>
<td>42</td>
<td>2,044</td>
<td>380</td>
<td>115</td>
<td>176</td>
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<td>1987-88</td>
<td>2,627</td>
<td>45</td>
<td>2,129</td>
<td>396</td>
<td>126</td>
<td>-21</td>
<td>3,439</td>
</tr>
</tbody>
</table>

* At a rate of 3 per cent on the growth in the Fund and including £25 million assumed to be interest on the National Superannuation Fund's share of the balance in the existing National Insurance Funds.

† In addition to the part of the existing National Insurance Funds transferred to the National Superannuation Fund.

14. As mentioned in paragraph 12 above, contracting out would lead to an immediate reduction in contribution income and a consequent saving in benefits emerging only gradually. The period during which the National Superannuation Fund will continue to increase will, therefore, be reduced to an extent depending on the numbers of employees who are contracted out, the amount of the reduction of contributions and, to a smaller extent, on the terms finally agreed for relating the reductions of pension to those of contributions. For example, for those at present contracted out (i.e. some 4½ million men and ½ million women), each ½ per cent a side reduction in the contributions would reduce the period of growth of the fund by about ½ years, and the maximum size of the fund would be correspondingly reduced.

15. The estimates of growth in the fund given in Table 7 and in paragraph 14 above are necessarily speculative, since its progress will be very sensitive to changes in benefit costs and contribution yields which might result from causes other than contracting out. For example, costs of pensions can be affected by changes in pensioners' mortality rates or by patterns of retirement; and in so far as the rate of augmentation of benefits in payment over a period might differ from the rate of increase of earnings, there would be a departure from the relative position shown on the basis of constant earnings.

**Future changes in contribution rates**

16. The financial position of the scheme will have to be examined from time to time and adjustments to contributions or benefits may be necessary to meet changing circumstances. In any event it is to be expected that an increase in contribution rates will be required for the National Superannuation Fund when the annual income begins to fall short of outgo. An indication of the contributions needed to meet the costs on a pay-as-you-go basis is given in Table 8, which sets out the percentage rates of contribution for certain years assuming that Exchequer supplements are payable at the present proportions. The rates represent the total rates for employees and employers jointly (the employees' rate being subject to a ceiling) on the assumption of constant earnings, but can be assumed to show the rates that would be needed if benefits as well as contributions were to rise in line with earnings. No allowance has been made for interest on the fund built up from the surpluses expected in the early years, but Table 7 shows that interest income would be relatively small in relation to benefit expenditure.
TABLE 8
Estimated joint rates of contribution from employed persons and employers which would be required to finance the National Superannuation Fund on a pay-as-you-go basis in certain years

<table>
<thead>
<tr>
<th>Year</th>
<th>Rate of contribution (employee and employer jointly)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Per cent</td>
</tr>
<tr>
<td>1972-73</td>
<td>7.7</td>
</tr>
<tr>
<td>1977-78</td>
<td>8.4</td>
</tr>
<tr>
<td>1982-83</td>
<td>8.9</td>
</tr>
<tr>
<td>1987-88</td>
<td>9.7</td>
</tr>
<tr>
<td>1992-93</td>
<td>10.4</td>
</tr>
<tr>
<td>1997-98</td>
<td>11.1</td>
</tr>
<tr>
<td>2002-03</td>
<td>11.4</td>
</tr>
</tbody>
</table>

Notes
(i) The rates in this table do not allow for contracting out (see para. 17 below).
(ii) The initial joint rate proposed is 9\(\frac{1}{4}\) per cent (4\(\frac{1}{4}\) per cent subject to a ceiling for employees and 4\(\frac{1}{4}\) per cent with no ceiling for employers).

17. It follows from paragraph 16 above and Table 8 that, before allowing for contracting out, the joint rate of contribution for the National Superannuation Fund (initially 9\(\frac{1}{4}\) per cent of earnings) might have to be raised to about 10 per cent after 20 years and to about 11 per cent by the end of the century. Contracting out would result in a loss of contributions which for the years shown would exceed the saving in benefit expenditure so that the rates in the table might be too low to an extent depending on the numbers contracted out, the rate of increase in earnings, and the terms which might be agreed for the reductions of contributions and pension. With the present proportions contracted out the shortfall in the rates of contribution might be of the order of 0.1 per cent of earnings for each \(\frac{1}{4}\) per cent a side by which the rate of contribution was reduced.

18. Even after 30 years, some pensions in payment will be based wholly or partly on the flat-rate benefits of the present scheme and it is estimated that the average pension in payment will still be some 10 per cent lower than the full rate under the new scheme. Other things being equal, therefore, the joint rate of contribution required for the National Superannuation Fund would probably have to be increased by a further 1 per cent of earnings (\(\frac{1}{4}\) per cent a side) over the early part of the next century to deal with this feature. The actual rate of contribution required at any time, however, is determined not only by the degree of maturity of the scheme and the other factors referred to in earlier paragraphs, but also by the relative numbers of pensioners and contributors. Estimates for the more distant future will depend to an increasing extent on the numbers of future births and any estimates of rates of contribution for periods more than 30 years ahead would be very speculative.

19. The effect of many of the factors which will play an important part in the development of the scheme will not become clear until it is brought into force. For example, the extent to which employers will take advantage of an option to contract out of part of the retirement pension and the age and salary after consultation with interested parties. Similar uncertainty applies to the provision under which voluntary contributions will be paid by workers with very low earnings and others outside the scope of compulsory contributions. The whole pattern of claims, particularly for benefits in the Social Insurance Fund, may well be changed by the new benefit provisions and in particular by the inclusion of all employed married women. It will, therefore, be necessary to follow the development of the scheme and the level of claims particularly carefully during the early years.

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