INTRODUCTION

The attached draft White Paper was discussed at Home and Social Affairs Committee on 15 June, and approved for submission to the Cabinet. This memorandum discusses points to which my colleagues may wish to give particular attention.

CONTRIBUTION CHANGES (paragraphs 18-22, 38-34 and Appendix 1)

2. The White Paper emphasises the need for a realistic and fair approach to meeting the rising cost of retirement pensions but it is difficult to give people a true picture of how the change will affect them personally in four years' time. Broadly speaking, employees on average earnings will, from September 1971, be paying about the same in flat-rate and graduated contributions as they will eventually be paying in earnings-related contributions under these proposals. The lower-paid will pay less in 1975 than they do now. The higher-paid will in general pay more, but by holding flat-rate contributions steady and raising the money for this year's uprating through graduated contributions we have brought the contracted-out man who will be exempt from the reserve scheme to within 12p of the amount he would be paying under the new scheme at the 1971 earnings ceiling of £42. (In what should be the comparatively rare case of the reserve scheme member earning £42 a week or more the increase would be 48p, but the extra contributions would of course provide him for the first time with an earnings-related pension on occupational scheme lines). The amount of the increase in 1975 for people earning more than £42 will depend upon movements in the earnings ceiling between now and 1975, but 1973, when benefits and contributions are due to go up again, will provide a staging-post which we shall use to bring people as near as possible to the levels of the new scheme.

THE SELF-EMPLOYED (paragraphs 43-45 and Appendix 1, Table 4)

3. The 5 per cent surcharge on Schedule D earnings will not be popular with the 600,000 or so self-employed affected but it is essential to ensure that they do not pay substantially less than the contributions to be paid for
employed persons with similar earnings. The scope for increasing the flat-rate contribution is limited because many self-employed people with low incomes could not afford to pay and would thus be deprived of benefit cover.

EXTRA PENSION EARNED BY POSTPONING RETIREMENT (paragraph 32)

4. I am proposing that the extra pension ("increments") earned by deferring retirement beyond minimum pension age should, for the first time, be covered by the (biennial) increases in the basic pension to maintain their purchasing power.

EXEMPTION FROM THE RESERVE SCHEME (paragraphs 55-62)

5. To meet the views of the pension interests I have made a change in the test of adequacy which occupational schemes will have to satisfy for exemption from the reserve scheme: they will be tested by reference to their benefits not their contributions.

FORM OF THE RESERVE SCHEME (paragraphs 71-74)

6. The Life Offices want the reserve scheme guaranteed return to be the same, whatever the age at which the contributions are paid, leaving it to the bonuses to enhance the return on contributions paid earlier in working life. They fear that many employers will otherwise be induced to "live on top" of the reserve scheme rather than rely entirely on occupational schemes. This view is not shared by the majority of those I have consulted from the National Association of Pension Funds; and the Government Actuary strongly advises against changing the reserve scheme in this way. I am satisfied that we should propose a fully age-related scheme, which will be manifestly fair to each contributor however long or short his period of membership.

RESERVE SCHEME FUND (paragraphs 75 and 76)

7. Expert advice on the possibility of requiring the Management Board to make their investment through a number of independent agencies is that this, apart from raising awkward problems of accountability, would not be technically sound. It could lead to competition for short-term results detrimental to the long-term interests of the scheme. We considered the use of two agencies rather than several: but the basic difficulties still remain and I have concluded that the Board must have freedom to settle its own investment arrangements. The safeguards would lie in appointing a strong Board, in requiring them to conduct their investments so as to secure the best pensions for scheme members and in limiting the voting equity they can hold in any one company. The last of these safeguards to some degree qualifies the obligation embodied in the second; but it imports an essential reassurance and should still allow of a well-balanced portfolio. The decisions about reserve scheme investment are relevant to the enquiry now going on into the future of the Public Trustee Office, and I shall be keeping in touch with the Lord Chancellor about this.
CONCLUSION

8. It is important for the successful launching of our proposals that they should now be made known as soon as possible and I invite my colleagues to approve the draft White Paper, subject to minor editorial amendments, for publication on Tuesday 13 July. I also invited their approval for preparation of the necessary legislation for presentation in the 1972-73 Session.

K J

Department of Health and Social Security SE1

25 June 1971
STRATEGY FOR PENSIONS

The Future Development of State and Occupational Provision

Presented to Parliament by
by Command of Her Majesty
1971

LONDON
HER MAJESTY'S STATIONERY OFFICE
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INTRODUCTION

1. This White Paper sets out the Government's proposals for implementing their policy on pensions. It is a plan for action which recognises the different purposes of the State basic scheme and of occupational pension schemes and the importance of establishing a framework within which each can fulfil its own function. Successive Governments have adapted the national insurance scheme to meet changing circumstances but there has been a growing realisation that more fundamental changes have to be made.

2. There are nearly twice as many retirement pensioners today as there were when the present national insurance scheme started in 1948 and the number is still rising. This means that costs are going up all the time. And since the number of pensioners is rising faster than the number of people at work these higher costs must fall even more heavily on the current working population. A scheme based on flat-rate contributions cannot meet the cost without causing hardship to workers on low earnings. It is time to face these facts squarely. The cost must be shared fairly and realistically. There must be no promises that depend on our children doing more for us than we are willing to do now for our parents.

3. Over the same period an equally remarkable growth has taken place in the provision of occupational pensions: about twice as many people today have pensionable jobs. More and more employers and employees have seen the wisdom of contributing to schemes which will lead to better living standards in retirement. Higher earnings have made this possible for many people who would formerly have been wholly dependent upon the State when they retired. The occupational pensions movement is an established and healthy part of our social system and through the savings they generate occupational pension schemes are playing a valuable part in our economy. It is time to welcome them into full partnership with the State scheme and to develop the scope they offer for greater independence in retirement.

4. From this background of rising costs in the State scheme and growing opportunities for occupational provision two clear objectives emerge. First, we must establish the State scheme on a sound financial basis which will enable rising costs to be met without hardship to contributors with low earnings. This means that contributions must be related to earnings. But to induce acceptance of earnings-related contributions by promising earnings-related pensions on a pay as you go basis would simply force the percentage rates of contribution to rise higher and higher to meet the emerging cost. This would be to solve the present financial problem by creating an even bigger one for the future. In the Government's view an equitable and enduring solution can only be found in a system of earnings-related contributions for basically flat-
rate pensions. Secondly, we must secure, primarily through the growth of occupational pension schemes based on funding principles, that everyone has the opportunity of saving for a pension related to his earnings and we must ensure that a change of job does not lead to the loss of occupational pension rights.

5. People are more likely to understand and accept the social rights and obligations that lie at the heart of the State scheme and to take full advantage of the opportunity for personal saving that occupational schemes offer if the essential difference between the two forms of pension is clearly recognised. The contrast is between, on the one hand, a State scheme through which today’s contributors support today’s pensioners and, on the other, occupational schemes through which today’s contributors by their savings can make their own personal provision for their own individual retirement over and above the basic State pension. The structural changes in the State scheme needed to put the Government’s policy into operation and the measures needed to provide greater opportunities for earnings-related pensions are described in the chapters that follow.

6. The present state of uncertainty about the development of State and occupational pensions has lasted too long and must be brought to an end. Pension provision can only thrive when there is confidence in the future. It is for the Government to show the way by declaring the main objectives. But there must be time for people to consider and discuss the proposed ways of achieving them. In the months ahead the Government will welcome constructive criticism from any source and they will be consulting a wide range of organisations representing employers and employees and the occupational pensions movement on the details of the proposals.

7. Following this period of consultation the Government will present a Bill to Parliament to give legal effect to their proposals. Their aim is to bring the main structural changes into operation from April 1975. Meanwhile, within the limits of the existing structure, the Government will press on with developing the State scheme. Action has already been taken to protect the purchasing power of the basic rate of pension and to pay for it without putting up the contributions of employees with low earnings. A start has been made with selective additions to the basic benefits in the State scheme so that the groups who are least able to look after themselves get preferential treatment. It is equally important that employers and trade unions, and the occupational pensions movement, should make the most of this opportunity for improving and extending occupational pension schemes.
CHAPTER 1

Objectives and Opportunities

8. The main objectives of the Government’s policy are:—

(1) To clarify the essential differences between State and occupational provision and to establish conditions in which each can develop in the way best suited to future obligations and opportunities.

(2) To provide through the State scheme a firm foundation of basic benefits paid as of right in return for contributions, with additional benefits for special groups so that priority needs are met by priority action.

(3) To safeguard the living standards of pensioners and other beneficiaries in the State scheme by a system of regular increases in benefit rates which will, as a minimum, maintain their purchasing power.

(4) To establish the finances of the State scheme on a sound basis by providing an equitable and buoyant source of contribution income without the need to put up contribution rates every time benefits are increased.

(5) To simplify the collection and recording of contributions in the State scheme, taking full advantage of labour-saving techniques.

(6) To give every employee the opportunity to build, on the foundation of the State scheme, an earnings-related pension for himself or his widow through an occupational pension scheme or, failing that, a State reserve scheme.

(7) To ensure that a change of job does not mean the loss of occupational pension rights.

(8) To set up an Occupational Pensions Board for the effective and flexible administration of the new provisions affecting occupational pension schemes.

1. A new relationship

9. The central issue for the future is how to shape the relationship between the State scheme and occupational schemes so that each form of provision is free to develop in the way that suits its essential characteristics. In the Government’s view this issue can only be satisfactorily resolved by a partnership in which the State scheme provides basic pensions and occupational schemes provide pensions related to earnings. The State scheme is the medium through which resources are transferred from people in work to those who have retired or are otherwise unable to work. It is a social scheme in which the range and level of benefits can and should depend upon social considerations and improvements in benefits can be shared with past contributors who are now the beneficiaries. The contributions needed to pay for, and establish a right to, these benefits
are a social obligation that can be recognised more clearly and accepted more readily if it is not confused with the principles of insurance.

10. By contrast the essential role of the occupational scheme is to enable an employee to secure higher living standards for himself and his family in retirement by setting aside a part of his earnings. It is becoming increasingly recognised that wages are only one aspect of the total remuneration the employee gets for his services: pension rights should be as much a part of the terms of employment for the shop-floor worker as for the top executive. So a system where each form of pension is true to its own purposes holds out the best prospect of combining intelligibility with flexibility. The present overlap has led to a rigid and complex system which cannot respond to new demands and is unnecessarily difficult to understand.

11. The present graduated pension scheme broke new ground by introducing an element of earnings-relation into State pensions ten years ago and, through the system of graduated contributions which successive Governments have extended, provided an additional source of income to help meet rising costs. It also paved the way for the future by recognising the important role of occupational schemes and stimulating their growth. This has now reached a point where it is to the advantage of both forms of provision that their future development should be along separate lines.

2. Priorities

12. National insurance benefits are often discussed solely in terms of retirement pensions. This does less than justice to the full range of benefits but it emphasises the fact that pensions must be at the heart of any reconstruction of the State scheme. The crucial financial and economic considerations for any Government lie in the emerging cost of retirement pensions. The growth in this cost will continue because the number of people over pensionable age will continue to rise for some years ahead. Moreover, even as a proportion of the population of working age the number over pensionable age has not yet reached its peak. The table below shows that it will be a higher proportion than at present for the next twenty years, but by 1996 it will have come down to below its present level. This turn of events, which has not been experienced in this country for many years, holds out a real prospect that after the next decade it will be possible to contain the previously inexorable rise in the cost of the basic scheme. There will then be scope either to reduce the general level of contributions or to increase the range and level of benefits. The choice is one to be made when the time comes; it must not be pre-empted by commitments entered into now.
### Population (Great Britain)

**Men aged 65 and over; women aged 50 and over**

<table>
<thead>
<tr>
<th>Year</th>
<th>Total (thousands)</th>
<th>As a percentage of total population</th>
<th>As a percentage of population of working age</th>
</tr>
</thead>
<tbody>
<tr>
<td>1948</td>
<td>6,448</td>
<td>13.2</td>
<td>20.4</td>
</tr>
<tr>
<td>1971</td>
<td>8,761</td>
<td>16.1</td>
<td>26.8</td>
</tr>
<tr>
<td>1976</td>
<td>9,296</td>
<td>16.6</td>
<td>28.9</td>
</tr>
<tr>
<td>1981</td>
<td>9,539</td>
<td>16.7</td>
<td>28.7</td>
</tr>
<tr>
<td>1986</td>
<td>9,671</td>
<td>16.5</td>
<td>28.3</td>
</tr>
<tr>
<td>1991</td>
<td>9,660</td>
<td>16.0</td>
<td>27.5</td>
</tr>
<tr>
<td>1996</td>
<td>9,482</td>
<td>15.2</td>
<td>25.9</td>
</tr>
<tr>
<td>2001</td>
<td>9,346</td>
<td>14.5</td>
<td>24.4</td>
</tr>
</tbody>
</table>

The population of working age has been taken as men and women over minimum school-leaving age and below pension age (65 for men, 60 for women). The figures from 1971 onwards are based on projections of the Registrar General's estimates of the mid-1970 population. Account has been taken of the raising of the school-leaving age in the 1972-73 school year.

**13. The level of basic pension.** In a scheme where the basic pension is flat-rate the level of the pension is crucial. It will inevitably be compared with supplementary benefit standards. From the end of September this year the standard rate of retirement pension for a single pensioner will be £6 per week; the supplementary pension for a single householder, including the long-term addition but excluding rent, will be £6.30. If the average rent allowance (about £1.85 a week in 1970) is included, a single pensioner on supplementary benefit gets on average about £8 a week in all. Thus the average gap between the two pensions is about £2 a week. In theory it would be an attractive proposition to close this gap so that contributory pensions did not fall short of the average standard of supplementary pensions. But in reality this would present an acute dilemma. About 30 per cent of retirement pensioners are getting a supplementary pension. Obviously the value of supplementary benefits could not be allowed to decline in order to enable national insurance benefits to overtake them. Maintaining the value of supplementary benefits must always be the first priority and this means that the gap could only be closed by increasing the value of contributory benefits by about one-third. In current terms this would involve increased expenditure of about £700 million a year for retirement pensions alone; for all benefits the extra cost would be about £1,000 million a year. A large increase in contributions would be required and most of the extra benefit would go to people with incomes above the supplementary benefit level.

**14.** Even if resources were available for such a massive increase on top of existing commitments the Government could not accept that this was the right order of priorities. Nor would it be right to go to the other extreme and neglect contributory pensions in favour of supplementary pensions. To do that would sap the enterprise of those who are in a position to do more for themselves. It would be damaging to the development of occupational pensions and other forms of saving for retirement if they did not offer the prospect of living
standards in later life above the level of supplementary benefit. The main function of the State scheme must therefore be to provide basic pensions, paid as of right in return for contributions and free from any test of means, at a level which recognises the realities of the situation. Improvements in the present level of the basic pension, beyond those needed to protect its purchasing power, must depend upon economic and other circumstances and the assessment of priorities by the Government of the time.

15. Selectivity. In addition to the basic pension the State scheme will continue to provide a wide range of other benefits and this will be extended, as the Government have already proposed, to contingencies that have not been previously covered. But not all the benefits of the scheme have to be paid at the same rate. Higher benefits for people with dependants are a long-established form of selectivity in the scheme. There is also preferential treatment of widows. The Government propose to develop the scheme further along selective lines with social priorities, not earnings, as the criterion for higher benefits. On the firm foundation of the universal basic benefits special provision will be made for those groups with a special claim on national resources. The very old, the severely disabled and those whose working life is cut short by chronic sickness stand out as groups for whom everyone would like to do more. An important feature of the Government’s approach is that the improvements they have already introduced, such as attendance allowance, invalidity benefit, pensions for younger widows and new benefits for the over eighties provide help now for those who are already disabled, chronically sick, widowed or very old, without having to wait for new rights to mature.

16. Supplementary benefit. The combination of contributory benefits founded on a basic pension with selective additions for categories of social need and occupational pensions related to earnings will provide independence in retirement, without recourse to supplementary benefit, for a steadily increasing proportion of the community. In the Government’s view it is right that the generality of people who are able to make better provision for themselves should be encouraged to do so in ways best suited to their circumstances. The measures proposed by the Government for this purpose are described later in this White Paper. For those whose resources still fall short of an acceptable minimum standard of living the Government will continue to maintain the provision that is made through the supplementary benefit scheme. For the immediate future, elderly widows must form a considerable proportion of supplementary pensioners. This is because women generally live longer than men and occupational provision for them has not developed to the extent that it has for men. Better pension provision for widows, related to their husband’s earnings or their own, must necessarily be a long-term prospect. The best way to help them now is to make special provision for the over-eighties, as the Government are doing, in both the basic and supplementary benefits schemes. This the Government are doing. It is inherent in the Government’s approach that their proposals do not provide a short-cut to a substantial reduction in the number of those who will qualify for supplementary benefit. The Government have firmly rejected any attempt to achieve this by seeking to impose on future contributors a bigger burden of State pensions than the present generation are prepared to support.
3. Safeguarding the value of benefits

17. Pensioners and other beneficiaries must be assured that their living standards will be properly protected and uncertainty about arrangements for maintaining the purchasing power of benefits must be removed. Legislation will therefore lay down a firm pattern of upratings every other year, designed at least to preserve the value of the basic pension and related benefits. Beyond this guarantee, as already explained, the extent of increases in benefits must continue to be determined by the Government of the time in the light of prevailing economic and other circumstances.

4. A sound and fair financial basis

18. The present contribution structure of the national insurance scheme has developed through changes which, though justifiable in themselves, have failed to produce a sound and sufficiently buoyant source of income. Equity and good administration alike demand the establishment of a simpler and better system which will enable the scheme to meet rising costs without having to put up the rates of contribution every time benefits are increased.

19. From the present hybrid system of flat-rate and graduated contributions the obvious and necessary step is to a single system of contributions related to earnings as the main source of finance for the scheme and as the basis of entitlement to benefits. This will enable the burden to be distributed more fairly than it is now without departing from the contributory basis of the scheme. The Government attach great importance to retaining the contributory principle. It is not, and never has been, an insurance principle in the commercial sense. But it does nevertheless serve a number of important purposes. It governs the conditions on which benefits are payable and ensures that benefits go only to those who have sustained their membership of the scheme. It gives people confidence that, through the payment of their contributions, they can establish a right to benefit that will be honoured when they are unable to work and when the time comes for them to retire.

20. In the present scheme flat-rate benefits are now financed to an increasing extent by earnings-related contributions. The Government's proposals rationalise and make explicit what has evolved from the logic of events. Current contributions have to be used to pay for current benefits. This is the social obligation that has to be met and the advantage of earnings-related contributions is that they enable it to be met more fairly and more efficiently. But if the shift of the cost of basic benefits to the higher earner is not to move too far into the province of taxation, the extent of redistribution in the contribution structure has to be limited. There will therefore be an upper limit of earnings above which further contributions will not be payable. For practical reasons there will also have to be a minimum level of earnings below which contributions will not be payable.

21. It may be argued that the significance of the contributory principle has now been reduced to the point where the Government should abandon it altogether in favour of a tax-based scheme. Contributions are a form of social security tax and there would be some advantages to be gained by completely severing the link between contributions and benefits: without the need for
individual records of contributions the scheme would be simpler and cheaper to run. The Government have examined this possibility. It would amount to much more than a change of name and a simpler form of administration. The repercussions would be far-reaching and costly. It would become necessary, eventually if not immediately, to pay benefits to people who do not contribute to the present scheme. The additional cost of paying basic pensions to everybody at pension age simply on a test of residence would be about £500 million a year. (The main reason for this is that, under the contributory system, wives do not get the standard rate of pension at age 60 unless they have qualified for it through their own contributions.) It would also be expensive in terms of both benefit and manpower to provide short-term benefit cover to nearly 4 million married women in employment who at present choose not to contribute to the scheme and are consequently not eligible for these benefits. Furthermore the administrative savings that might be expected to accrue from a tax-based system would be much diminished by the continuing need for individual records for the purposes of controlling claims to short-term benefits and administering a State reserve scheme of earnings-related pensions for employees without occupational cover. These are formidable objections to the abandonment of the contributory principle. Recognising the positive advantages that it has to offer, not least as a reaffirmation of public faith in the security of benefit rights, the Government have decided that it is necessary and right to retain it.

5. A simplified system of collection

22. The system of flat-rate contributions with which the present national insurance scheme began has become more complicated over the years by the addition of graduated contributions which have assumed increasing importance in the finances of the scheme. It has not been possible to increase the flat-rate element sufficiently to meet rising costs without bearing too hardly on the lower-paid workers and the continued existence of flat-rate contributions has become a hindrance to further development. Furthermore, the dual system of assessment and collection is cumbersome and inefficient. The Government's proposal to abolish stamped cards for employed persons and to collect their contributions entirely through the PAYE income tax system will provide a much needed simplification which will enable full advantage to be taken of technical developments over recent years, such as computerised payrolls. This will benefit all concerned: employers, employees and Government Departments. Self-employed and non-employed people will be able to pay their flat-rate contributions by means of stamped cards which for most of those concerned is likely to remain the most convenient method of payment. Studies are being carried out into the practicability of alternative methods of payment for those who find the stamped card inconvenient.

6. Earnings-related pensions

23. The security of a guaranteed basic pension through the State scheme is essential, but it is not enough. Every employee should have the opportunity to qualify for additional provision related to his earnings. A number of arguments have led the Government to conclude that for the great majority of people this can best be achieved through the expansion and improvement of occupational schemes.
24. First, there is the impressive record of growth of occupational schemes even at a time when the conditions for their maximum development have been lacking. A new survey of schemes will be undertaken before legislation is introduced; meanwhile projections based on the existing evidence suggest that perhaps 12 million employees are members of occupational schemes (70 per cent of male employees, and 30 per cent of female employees); and the value of occupational scheme funds amounts to some £10,500 million. Secondly, pension provision made through occupational schemes can be more closely adapted to the varying circumstances of people in different employments than would ever be possible under a State scheme. Thirdly, many employees place great value on the backing for their future pension which is provided by the setting aside of money from profits and earnings in a funded occupational scheme.

25. Despite their development over recent years, occupational schemes do not yet provide a sufficiently comprehensive answer to the need for earnings-related pensions. To encourage their further development is one of the prime purposes of the Government’s proposals. At present, the “white collar” worker is more likely than the “blue collar” worker to be a member of an occupational scheme—and men are more likely to be members than women. The benefits provided by some schemes, even after many years of service, are meagre. Cover for widowhood and provision for benefits to be increased after award, while improving, still leave much to be desired. The mere existence of an occupational scheme is therefore not enough; it should provide at an adequate level for at least a prescribed range of contingencies.

26. There would be no prospect of introducing and enforcing a statutory obligation on all employers to provide occupational pension cover, up to a prescribed standard, for every man and woman in their employment. Among small employers only a minority feel able to operate occupational schemes at present, and even employers with well-developed schemes would often find it impracticable to extend them to cover all their employees, including those who serve for only a short period. Adequate occupational cover for everyone is not therefore in sight.

27. It follows that although the Government propose to rely primarily on occupational schemes for the provision of earnings-related pensions, they must also provide earnings-related cover under a State reserve scheme for those employees without adequate occupational cover. This reserve scheme has to be designed for employers who cannot easily run an occupational scheme and its contributions must be no higher than the generality of such employers and their employees can afford. The scheme must therefore be of modest dimensions. It is in no way intended as a rival to occupational schemes or a substitute for their expansion. It also follows that those occupational schemes which have not already reached an adequate standard in the types and amounts of benefit they provide must be encouraged to do so.

28. Employers with occupational pension schemes which satisfy the minimum requirements to be laid down will be able to obtain complete exemption from the State reserve scheme in respect of employees covered by their schemes. These requirements and the form of the reserve scheme are discussed in more detail in paragraphs 55-81.
29. The new arrangements for earnings-related provision will supersede the present graduated pension scheme which will therefore be wound up. The benefits rights earned under it will be preserved.

7. Preservation of occupational pension rights

30. A continuing weakness of many otherwise good occupational schemes is that members who leave before pension age, for instance on a change of job, frequently lose or abandon their pension rights. At present only an estimated 40 per cent of employees who leave early have the opportunity of retaining their pension rights, and the majority even of them choose not to do so. The Government regard it as essential that people who are building up pension rights in an occupational scheme should not be deprived of those rights merely because they leave before pension age; the proposed legislation will ensure this. Furthermore reliance on pensions from occupational schemes as an integral part of provision for retirement cannot be reconciled with the refund of relevant contributions paid after the start of the new arrangements. The Government have therefore concluded that it should not be open to leaving employees to surrender, for a cash refund, preserved pension rights which derive from service after the new arrangements take effect.

8. The Occupational Pensions Board

31. To implement these plans for stimulating the further development of occupational pension schemes, an Occupational Pensions Board is to be established. The Board's functions will be to accord "recognition" to occupational schemes of the required standard, so as to exempt the members and their employers from contributing to the State reserve scheme; to supervise the arrangements for preserving the pension rights of early leavers; and to assist occupational pension schemes to change their rules, if they need help in doing this, to adapt to the new situation. The Board will be an independent authority with statutory powers, and will include members appointed after consultation with employers' and employees' organisations as well as other members appointed for their special knowledge and experience of pensions matters. Within the statutory framework laid down, the Board will have discretion to conduct their affairs flexibly and to follow whatever procedures they find best adapted to the varying circumstances of the cases with which they are called upon to deal. The Board's functions will supersede those of the present Registrar of Non-Participating Employments (although they will have wider responsibilities) and they will take over the powers now exercised by the Chief Registrar of Friendly Societies for facilitating modification of the rules of occupational schemes. The Board's role will not only be one of supervision and, where appropriate, adjudication (for example, they will formally determine whether a scheme's rules provide satisfactorily for early leavers); they will also be available to give informal advice and guidance on matters within their sphere of responsibility. The Government are confident that in all these ways the Board will play an important part in ensuring the effective introduction and smooth operation of the new arrangements.
CHAPTER 2

The Government's Proposals
The State Basic Scheme

Benefits

32. Retirement and widows' benefits. The earliest age for payment of the State retirement pension will remain 65 for men and 60 for women, subject as now to the condition that the claimant has actually retired. Those who defer retirement after pension age will continue to earn extra pension: these increments will not remain fixed in money terms as they are now but will be brought within the arrangements for two-yearly increases along with the basic pension (see paragraph 33). The pensions of those who retire but subsequently have substantial earnings will still be subject to an earnings rule until age 70 (men) and 65 (women), but the operation of this rule will be modified from time to time. Widows’ benefits will be payable in the same circumstances as at present, including the modified rates of pension for women widowed between the ages of 40 and 50. Arrangements have already been made to extend to women who become divorced under the age of 60 the right that a widow has to use her former husband’s contribution record for the period before as well as during the marriage if this would improve her retirement pension.

33. The Bill introducing the new structure will bind the Government to review basic pensions and related benefits every two years and to increase them by amounts sufficient at least to maintain their purchasing power. The Bill will also provide for these benefit increases to be achieved in future by regulations, thus avoiding the need for fresh legislation every two years. Similar arrangements for biennial increases are envisaged for industrial injuries benefits, and for war pensions.

34. Invalidity benefit. At present people who are incapable of work are normally eligible for sickness benefit from the early days of incapacity and can continue to draw it until retirement pension replaces it. It has become increasingly clear, however, that chronic sickness is a very different contingency from short-term sickness involving only a few weeks away from work. This is being recognised in the improvements in benefit for the chronic sick due to take effect in September this year. These will radically alter the present position: for some people it will be completely transformed. There will be special additional payments of invalidity allowance related to the age at which incapacity began; easier and more flexible conditions for benefits where an invalidity pensioner’s wife goes out to work; and higher benefits for dependent children. The emphasis is being placed on those who become chronically sick at a fairly early age: these are the people who suffer the greatest loss of opportunities by comparison with their contemporaries.

35. Attendance allowance. Arrangements have also been made for the introduction of a new benefit for very severely disabled people. This is the attendance allowance of £4.80 a week which will become payable later this year to those who are most in need of special help because they are very heavily
dependent on the care of their relatives and friends. This is the first time that their special needs have been recognised in the State scheme. Experience with attendance allowance, and invalidity benefit, will guide the future development of provision for the chronic sick and disabled.

36. **Short-term benefits.** The structure of these benefits, covering sickness, unemployment and maternity, will need to be adapted to the new system of earnings-related contributions. Detailed proposals will be announced later.

37. **Industrial injuries benefits.** The changes outlined in this White Paper do not bear directly on the benefits of the industrial injuries scheme, although the improvements for the chronic sick, for example, have already led to corresponding improvements in them. The role of the scheme in providing benefits adapted to the needs of industrial casualties is in accord with the Government's general policy of selective provision for special groups. They propose to continue to develop the scheme in its own way, taking account of the changes being made in the wider context of the national insurance scheme.

**Contributions**

38. **Contribution structure.** The basic scheme will continue to be financed on a pay-as-you-go basis which means that the total contribution income required is determined by the current level of benefits and number of beneficiaries. The Government Actuary estimates that by 1975 a combined employer/employee contribution of about 12.5 per cent of reckonable earnings will be required (see Appendix 3). This will cover industrial injuries benefits and a contribution for the National Health Service but not the employer's contribution to the Redundancy Fund. The exact structure of contributions is dependent on a series of interlocking decisions, including in particular the allocation of the contribution in respect of employees between them and their employers; the role of the Exchequer (i.e., of general taxation); and the extent to which earnings-related can be extended to the self-employed.

39. **Employees' contributions.** There are at present two contributions for employed persons: a flat-rate contribution, collected either by means of stamped cards or by direct payment, and a graduated contribution collected through PAYE. From September 1971 the graduated contribution will be 4.75 per cent of earnings between £9 and £18 a week (0.5 per cent only for those contracted out of the graduated pension scheme) and 4.35 per cent of earnings from £18 to £42 a week.

40. This structure will be replaced by fully earnings-related contributions collected through PAYE. Employees with earnings below a minimum qualifying level (about one-quarter of average earnings*) will not be liable to pay earnings-related contributions but they will continue to be covered for industrial injuries benefits. They will also be able to pay flat-rate contributions voluntarily for pension purposes (see paragraph 46). Employees with weekly earnings above the minimum qualifying level will pay contributions at 5.25 per cent on all their earnings up to an upper limit which will correspond roughly with one-and-a-half times average earnings. They will cease to pay flat-rate con-

*Here and elsewhere "average earnings" is used 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's yearly inquiries into earnings.
Contributions will be assessed on earnings in the employee’s pay period as in the present graduated scheme so as to cater for employees who are not paid weekly. The changeover to earnings-related contributions is specifically designed to share the cost of the scheme more fairly. Thus the below-average earner will tend to pay less than before and the above-average earner will pay more. Appendix 1 contains tables illustrating, as at September 1971, the contributions which would be payable under the new scheme at various earnings levels compared with those payable under the present scheme. These comparisons do not, however, indicate the amount of the differences that will actually occur at the start of the new scheme since these will be affected by changes in the level of contributions needed to finance increases in benefit rates between September 1971 and April 1975.

41. Employers’ contributions. In the basic scheme, with an employee’s rate of contribution of 5.25 per cent, the balance of the joint contribution to be met by the employer will be 7.25\* per cent of his employees’ PAYE earnings assessed over the same range as the employee’s own contributions. The Government consider it right that under the new system employers should pay a rather higher proportion of the joint contribution than employees.

42. Exchequer supplement. The contribution from general taxation towards the cost of the present scheme amounts to about 18 per cent of the combined contributions of insured persons and employers. The Government propose to retain the Exchequer supplement at this level. As with employees’ and employers’ contributions, the income from it will rise as earnings levels rise.

43. The self-employed. Self-employed people, who number about 1\(\frac{1}{2}\) million and have a wide variety of occupations and incomes, pay only flat-rate contributions and receive only flat-rate benefits under the present scheme. It would be in keeping with the Government’s plans for the financing of the State scheme for them to pay fully earnings-related contributions. Unfortunately it is not practicable to set up a system of collecting fully earnings-related contributions from the self-employed which could serve as the basis of their entitlement to benefits. Self-employed people are generally assessed for income tax under Schedule D, not under PAYE to which the machinery for collecting earnings-related contributions is linked. Tax under Schedule D is not based on the current year’s earnings, as it is under PAYE, but is generally levied on the previous year’s earnings. There is inevitably a considerable delay before the agreed earnings for tax purposes for a particular year are known. Nor would the same figure necessarily be a realistic one for national insurance purposes: it would often take account of factors, such as the effect of capital allowances, which ought logically to be discounted in determining the amount of a person’s income in the context of the national insurance scheme. There is also the difficulty that many self-employed people who clearly have no liability for tax do not at present have their profits assessed at all; in these cases it would be necessary to make assessments purely for national insurance purposes. The contribution liability of the self-employed must therefore continue to be primarily flat-rate.

\*This does not include the employer’s contribution to the Redundancy Fund.
44. Reliance on flat-rate contributions means, however, that unless they could be set at a substantially higher level than before—with consequent hardship to those with small incomes—the contributions payable by the self-employed man with above average earnings would be much too low by comparison with the joint employer/employee contributions for employees with comparable earnings. The Government propose therefore that, in addition to a flat-rate contribution at about the present level, those self-employed people with Schedule D earnings exceeding £1,000 at present levels should pay an earnings-related contribution of 5 per cent on the excess up to the same annual upper limit as will apply to employees. (It would not be economic to levy an earnings-related contribution on Schedule D earnings below £1,000 a year.) Table 4 in Appendix 1 compares, as at September 1971, the contributions which would be payable by the self-employed under the new scheme with those payable under the present scheme.

45. The earnings-related contribution will be collected with Schedule D tax and paid in bulk to the National Insurance Fund as a general contribution towards the cost of the scheme. It follows that this form of contribution will not affect the self-employed person’s benefit; this will depend entirely on the flat-rate contribution. Self-employed people with low earnings will, as under the present scheme, be excused from the compulsory payment of flat-rate contributions although they may pay voluntarily if they wish, either at the self-employed or the non-employed rate. The position of those who are self-employed for national insurance purposes but are assessed for income tax under Schedule E will be determined later.

46. The non-employed. Under the present scheme people who do not normally work are liable to pay a special rate of contribution, for a limited range of benefits. But those with an income of £6 a week (£9 from September 1971) or less can apply to be excempted from liability. In the new system, in which contributions will generally be related to earnings, it would not be appropriate to continue compulsory liability for payment of contributions for those who have no earnings. Compulsory liability will therefore cease but arrangements will be made to enable those who wish to do so to continue to pay contributions voluntarily so that they can receive the benefits for which they had expected to qualify. Those who, though normally employed for some part of the year, have not paid sufficient contributions to enable them to qualify for the full rate of pension will also have the opportunity to pay. So will those who, though earning less than the minimum level for compulsory contributions, nonetheless wish to qualify for a basic pension. Contributions payable by people in these categories will be flat-rate at a level designed to secure entitlement to the standard rate of basic pension.

Married women and widows

47. The Government have decided that married women and those widows who are receiving benefit should continue to have the choice of not paying full national insurance contributions. Their employers will as now be liable to pay their own share of the contributions. It is true that the changeover to fully earnings-related contributions and the movement towards equal pay will remove the disproportionate contribution burden that the present flat-rate contribution would impose on these women, especially those who work part-
time, most of whom have much lower earnings than men. But many wives and widows work for only a part, and often only a small part, of their adult lives and the scheme provides a wife with a pension on her husband’s contributions. She can obtain no extra pension from her own contributions unless they are sufficient to earn more than she would in any event qualify for on his contribution record. In these circumstances nearly four million married women at present exercise their choice not to pay contributions. The Government consider that it would not be right to withdraw this element of choice and compel them to pay full contributions. It is only fair, however, that those who choose not to pay should be required to contribute towards the cost of industrial injuries benefits for which they will have cover and towards the national health service.

48. Self-employed married women and widows are in a different situation because they do not qualify for industrial injuries benefits and no employer’s contribution is payable. The administrative cost of making them pay a small flat-rate contribution towards the cost of the National Health Service would not be justified. It would not be right, however, for the higher earners among them to escape the payment of contributions altogether and it is therefore proposed that self-employed women who choose not to pay full contributions should nevertheless pay the 5 per cent earnings-related contribution which is to be charged on Schedule D earnings between £1,000 and the upper limit of the scheme.

Qualifying conditions for benefit

49. Entitlement to retirement pension under the present scheme depends upon the average number of contributions paid in each full contribution year between entry and age 65 (60 for women). A yearly average of at least 50 contributions is necessary for a pension at the standard rate; there are reduced rates if the average is less than 50 but more than 13. There are four contribution years for this purpose, beginning in March, June, September and December, each contributor being assigned one of these when he enters the scheme.

50. The change to earnings-related contributions payable through PAYE means that different arrangements have to be made. All employees will have the same contribution year, coinciding with the tax year which begins in April. Entitlement to basic pension will depend on paying contributions at or above a minimum qualifying level of earnings in each of a prescribed number of years. The minimum level for contribution liability and entitlement to benefit will be about one-quarter of average earnings, its amount in cash terms when the new arrangements start in 1975 depending on future movements of earnings. The new test will require contributions to have been paid at the minimum level for about nine-tenths of the years between entering the scheme and reaching pension age (65 for men, 60 for women). In terms of a full working life of 49 years for men and 44 for women this means contributing for 44 years and 39 years respectively, the difference taking account of the lower pension age for women. Reduced rates of benefit will be payable where there are fewer years in which the minimum level of contributions has been reached. For widow’s pension, the qualifying conditions will be broadly similar to those for retirement pension: the qualifying period being the years between the date of the husband’s entry into the scheme and the date of his death. For invalidity benefit, entitle-
ment will follow automatically where a sick person remains incapable of work after more than six months of sickness benefit.

51. For benefit purposes the flat-rate contributions of self-employed and non-employed people will be treated as equivalent to contributions at the minimum qualifying level of earnings required to secure entitlement to the standard rate of basic pension. In this way it will be made possible for those who pay flat-rate contributions to build up a combined record if they also have periods when they pay earnings-related contributions as employed persons.

Credited contributions

52. Because the qualifying conditions for pension will generally be rather easier than at present, arrangements for crediting contributions will be less important than they are under the present scheme. It will still be necessary, however, to ensure that benefit rights in the basic scheme are maintained when earnings are interrupted, for example by sickness or unemployment. Credits will still be awarded therefore in these circumstances and they will take the form of crediting the people concerned with having paid contributions on earnings at the minimum qualifying level.

Transitional arrangements

53. When the new scheme starts most people will already have rights and expectations under the present scheme, and arrangements must be made for these to be preserved. This will be done by converting the rights of existing contributors based on flat-rate contributions into corresponding rights based on earnings-related contributions: for example, by counting every 50 contributions paid under the present scheme as a year in which the minimum qualifying level of contributions has been reached under the new arrangements.

The graduated pension scheme

54. No new graduated pensions will be earned under the present arrangements after the start of the new scheme. Graduated pension already earned by April 1975 will be preserved and paid with the basic pension on retirement. The graduated pension scheme contains no provision for increasing the pensions awarded under it in the light of changing money values and it was on this basis that many employers took decisions on contracting out and designed their occupational schemes. The Government of the day gave explicit assurances that employees who were contracted out could not be made worse off as a result. To include these pensions in the system of two-yearly reviews of basic pensions would be unfair to the large number of people who have been contracted out because the Government could not make matching increases in their occupational pensions and could not impose such an obligation retrospectively on their employers. Graduated pensions must therefore continue to be paid in the money terms in which they will have been earned.

OCCUPATIONAL PENSION SCHEMES

Exemption from the State reserve scheme

55. An employer with an occupational scheme which is “recognised” as satisfying certain minimum requirements will be able to obtain complete exemption from the State reserve scheme in respect of all his employees who are members of
the occupational scheme. This should create a climate of opinion in which the normal job will be seen as providing not only a wage or salary but an earnings-related pension as well.

56. To enable employers and employees to understand fully what is at issue and to give occupational schemes freedom to grow and develop in their own way, it is important that the minimum standards required should be as straightforward as possible and that the Occupational Pensions Board (see paragraph 31 above) should be allowed a sensible discretion in administering them. Equally they must ensure that all employees in recognised schemes have appropriate pension cover, that their benefits are effectively secured and that the schemes themselves are designed, as the reserve scheme will be, recognition to provide widows' benefits as well as personal pensions.

Conditions for recognition

57. With these objectives in mind the Government have decided that, while the prime condition which an occupational scheme must satisfy for recognition should, as under the present contracting out arrangements, be related to the level of its benefits, the general approach should be both simpler and more comprehensive. On the one hand, there will be no attempt to impose a test of equivalence such as now exists; on the other, the conditions will not relate solely to the personal pension. Instead, it is proposed that, in order to get recognition, a scheme must provide both a personal pension for men at an annual rate of not less than 1 per cent of the PAYE earnings on which reserve scheme (and basic scheme) contributions will be payable, and a widow's pension payable at half the husband's pension rate. The death benefit must take the form of a pension if the husband dies in retirement but the scheme will have the option of paying a lump sum if he dies before retirement. The scheme will be required, subject to the alternative test outlined below, to maintain the value of the pension after award, for both pensioner and widow, on one of three bases: by linking the pension to the cost of living index; by providing for a prescribed rate of increase after award; or by satisfying the Occupational Pensions Board that reasonable financial provision is being made to ensure increases after award, without commitment to a specific rate.

58. As an alternative to guaranteeing post-award increases a scheme will be able to secure recognition if it offers a prescribed higher rate of personal pension. For example, if the prescribed rate of increase after award were set at 3 per cent a year the scheme might as an alternative be able to gain recognition if it provided a personal pension of at least 1.25 per cent of the relevant PAYE earnings for men with analogous provisions for widowhood. This alternative test is put forward because it would be unfair to make increases after award mandatory beyond the point at which the total pension in a scheme with higher rates of benefit was as good as the pension in a smaller scheme which did provide for such increases.

59. The minimum rate of pension required for women in recognised schemes will be lower than for men to take account of the fact that pension must be available to them from the age of 60 (compared with 65 for men) and their greater longevity, with an offset to allow for the absence of mandatory dependency provision. The figure proposed is 0.7 per cent if the scheme provides for increases after award on one of the three bases earlier described; but the
figure will be rather higher if post-award increases are not provided. The Occupational Pension Board will have discretion to accept a slightly reduced standard of personal pension for women in cases where the scheme gives the woman cover for dependency benefits, for example, in respect of elderly parents.

60. The standards for recognition should ensure that recognised schemes will be providing benefits which, taken as a whole, compare more than favourably with those in the reserve scheme.

61. **Security of benefit.** It is necessary to ensure that the benefits in recognised schemes have adequate financial backing. Under the existing arrangements for the financial supervision of “contracted out” schemes, if the scheme cannot assure the benefits and the employer fails to make a “payment in lieu” (which buys the employee rights in the State graduated scheme), liability falls in the last resort on the National Insurance Fund. Such a liability could not equitably be placed on the reserve scheme. The Government propose, therefore, that recognised schemes should have to be funded or insured up to the level needed to finance the benefits required for recognition as well as any pensions in payment and that benefits in these two categories should be given priority if for any reason the scheme is wound up. The Government appreciate, however, that a priority rule of this kind might not be acceptable to all schemes. It is envisaged that in such cases the Occupational Pensions Board will not require priority to be given provided that they are satisfied as to the scheme’s overall funding arrangements. The Board will continue to exercise supervision over any scheme which has ceased to be recognised, so as to safeguard pension rights up to the required minimum level which have accrued during the period of recognition.

62. **Time for adjustment.** In order to meet the new requirements many schemes, particularly those which do not provide widowhood benefits or any form of post-award increase, or which do so on an optional or discretionary basis, may be faced with the need to make substantial modifications. It is proposed that where legal difficulties stand in the way the Occupational Pensions Board should be enabled to facilitate such modifications (see paragraph 69 below). The possibility will be examined of empowering the Board to accord recognition to schemes in advance of the formal amendment of their rules on the basis of a binding declaration by the employer that the scheme will be operated in the interim as if the formal amendment had been made. The Government propose to take all possible steps to limit the administrative burden on schemes and their professional advisers, and to retain as much of the present procedure for securing recognition as accords with the new framework and with protecting the interests of those affected. In advance of legislation, the Government intend to discuss all these matters with representatives of occupational schemes and others concerned.

**Preservation**

63. Encouraging the expansion and improvement of occupational schemes has to be combined with steps to remedy one of the main flaws in existing schemes—the substantial loss of pension rights each year by people who leave their employment before pension age. There is general acceptance of the need for action in this field. Reliance on occupational pension schemes to provide
earnings-related pensions in retirement cannot be reconciled with a situation in which even longstanding members of pension schemes may forfeit their pension rights if they become redundant, have to give up work on account of ill-health or simply change their job. Ideally it should be possible for a person to take his pension rights with him, so that at the end of the day, no matter how many changes of job he has had, he gets a single pension from a single source; but the diversity between schemes makes this impracticable at present. The form of protection proposed, therefore, will be the provision of a deferred pension by the scheme which the employee is leaving; but there will be no bar to an employer offering, and the employee accepting as an alternative to a deferred pension, the payment of a transfer value to another scheme. Indeed it is hoped that preservation, when it is fully effective will encourage schemes to make more use of such transfer arrangements as a convenient means of discharging their liabilities under the legislation. The preservation proposals are planned to take effect from the same date as the main structural changes in the State scheme; a detailed description is in Appendix 2.

64. There are two important distinctions between the preservation part of the proposed legislation and the part concerned with recognition and exemption. Recognition and exemption focus on a minimum range and level of benefits which have to be provided under an occupational scheme if its members are to be exempted from contributing to the reserve scheme. Preservation is concerned with all schemes whether or not they are recognised for the purpose of exemption from the reserve scheme, and with the full range and amount of the benefits which the employee concerned has earned in respect of his service as a member of the pension scheme. The Occupational Pensions Board will be responsible for the operation of both sets of provisions; and one of its functions will be to see that schemes' rules are in line with the preservation requirements. Scheme members (and other interested persons) will have a right to apply to the Board if they consider there has been any failure to comply. Once a scheme's rules have been brought into line, it will be for individual members to enforce their rights where necessary through the scheme's own arbitration machinery, with recourse to the Courts as a last resort.

65. In order to qualify for a preserved pension an employee will have to have completed five years' pensionable service and attained age 26 before leaving the pension scheme. The legislation will be directed to ensuring that the early leaver gets his fair share of whatever range of benefits the scheme ordinarily provides. Both retirement benefits and widows' benefits payable on death after retirement will be covered, and with them any contractual provision in the scheme for the increase of pensions in payment.

66. Where an employee leaves a recognised occupational scheme after serving for less than five years then, unless his pension rights are preserved or transferred to another scheme, his employer will be required (subject to a de minimis rule to eliminate very small payments) to pay into the reserve scheme the total contributions which, but for exemption, would have been due for the period concerned.

67. Reliance on occupational pension provision as a central and expanding sector of the total provision for retirement could not be justified if job mobility, whether voluntary or enforced, continued to undermine it to the extent that
it does now. In the Government Actuary’s second survey,* published in 1966, it was estimated that about 90 per cent of all those who left pensionable employment before pension age lost their pension rights with their job, one-third of them choosing a refund of their contributions in preference to other options. The Government have therefore decided not to allow the refund of contributions as an alternative to a deferred pension in respect of a period of service of five years or more after the appointed day. This may be criticised by some as a restriction on choice; but in the Government’s view it would be wrong to allow pension rights earned after the legislation has come into force to continue to be sold away, with the possibility of unnecessary dependence on supplementary benefit paid for by the general body of taxpayers including the more provident members of occupational pension schemes. Pension rights in respect of service before the appointed day will also qualify for preservation, but the refund of contributions will continue to be permitted as an alternative.

68. Some employers may have held back from introducing preservation arrangements into their own schemes until they had a detailed account of the Government’s proposals. They should now be able to go ahead. For their own part, the Government intend to consult the relevant staff interests with a view to providing preserved pensions for those with the necessary qualifying service who leave the civil service or national health service schemes after a date well in advance of the date (April 1975) when the new legislation is planned to take effect. They will be considering from the same standpoint how soon preservation can be introduced into the armed forces schemes.

Modification of schemes

69. The Occupational Pensions Board will be empowered to authorise modifications of the rules of pension schemes where this is necessary to enable them to secure recognition; to comply with the preservation requirement; or to make provision for the pension rights of a leaving member to be transferred to another scheme or “bought out” by the purchase of a deferred annuity. This power will be restricted to cases where the scheme is unable to make the necessary changes under its own alteration procedures, or can only do so in an unduly cumbersome manner. There will be consultation with the interested organisations about any other circumstances in which the Board might need to be empowered to help schemes to adjust themselves to the new situation.

Approval of schemes by the Inland Revenue

70. The comprehensive tax reliefs given to approved pension schemes have been a major factor in their development, and the changes proposed in this year’s Finance Bill in the conditions for approval of occupational pension schemes for tax purposes introduced by the Finance Act 1970 reflect the importance the Government attach to the encouragement of occupational provision. The Inland Revenue approval is directed to the control of this tax relief and their rules are consequently concerned with the maximum contribution or benefit which can be allowed to escape the normal incidence of tax. The rules which the Occupational Pensions Board will be applying for the purpose of recognising schemes will be concerned with the minimum standard required for exemption from membership of the reserve scheme. The two sets of rules

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are thus differently orientated but both will exercise an influence on the direction, and to some extent the pace, of development of occupational pension schemes. Although it is not possible to make the Occupational Pensions Board responsible for both functions, since control of the tax reliefs must remain with the Revenue, the Board and the Inland Revenue’s Superannuation Funds Office will be concerned to work out the best way of co-ordinating their operations.

**THE STATE RESERVE SCHEME**

71. The reserve scheme will be entirely separate from the State basis scheme: it will be a funded scheme run on the lines of an occupational scheme by an independent Board of Management. Reserve scheme pensions will be assessed by reference to the contributions paid on behalf of each contributor so that he receives a fair return however long or short the period for which he and his employer contribute. Pension scales will be laid down showing by age and sex the amount of pension the scheme guarantees to pay for each contribution unit (see Appendix 2, Table 3). The scheme will also include a profit-sharing element enabling the benefits on the age-related scales to be enhanced periodically by “bonuses”. There will be a reasonable expectation that these “bonuses” will prove sufficient in amount to offset any price increases, and thus to maintain the real value of the pensions, though there will be no guarantee of this.

**Contributions**

72. Contributions to the scheme will be set at 4 per cent of the same range of PAYE earnings as basic scheme contributions; the employer will pay 2·5 per cent and the employee 1·5 per cent (see table below). Like basic scheme contributions, reserve scheme contributions will be collected through PAYE, but they will be paid over in bulk to the reserve scheme fund which will be under the control of the Board of Management. The Board will pay for the use of Governmental machinery in the collection of contributions and for any other services Government Departments may perform on its behalf. The employee’s contribution has been set at less than half the total partly so as to provide some measure of compensation for the absence of tax relief on his share: other considerations apart, treating reserve scheme contributions similarly to occupational scheme contributions in this respect would further complicate the PAYE system and increase the number of staff needed to administer it.

<table>
<thead>
<tr>
<th>Employees’ earnings £</th>
<th>Employee’s contribution £p</th>
<th>Employer’s contribution £p</th>
</tr>
</thead>
<tbody>
<tr>
<td>10</td>
<td>0·15</td>
<td>0·25</td>
</tr>
<tr>
<td>20</td>
<td>0·30</td>
<td>0·50</td>
</tr>
<tr>
<td>30</td>
<td>0·45</td>
<td>0·75</td>
</tr>
<tr>
<td>42</td>
<td>0·63</td>
<td>1·05</td>
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</tbody>
</table>

**Benefits**

73. The reserve scheme will provide both personal and widows’ pensions. The widow’s pension will be paid at half the rate of the late husband’s pension or, if he has died before pension age, at half the rate of the prospective pension
secured by the contributions he had paid up to the time of his death. Personal pensions will be paid at the age of 65 for a man, and 60 for a woman, irrespective of retirement. An earnings rule would not be appropriate in a scheme of this sort run on the lines of an occupational scheme, and a retirement condition needs to be supported by an earnings rule to be effective. Benefit under the reserve scheme will be treated in the same way as benefit under an occupational scheme in cases where entitlement to supplementary benefit is being assessed. All pension rights in the reserve scheme will be fully preserved: there will be no contribution refunds.

74. The amount of reserve scheme pension will depend not only on what contributions have been paid and the sex of the contributor but also on the age at which the contributions were paid (see Appendix 3, Table 3). The younger the contributor the longer the period up to pension age during which the contributions will accumulate at interest, and therefore the bigger the amount of pension for any given sum. Age-related benefits will enable widely varying periods of active membership to be accommodated in a manifestly fair way, whatever the age of the contributor. The tables below show what pension the reserve scheme might be expected to produce for contributors entering it at various ages. Table A shows the position at constant earnings—so as to provide a basis for comparison—and Table B is based on the assumption that real earnings increase by 3 per cent a year. Each table is based solely on the amounts of pension to be guaranteed by the scheme; and the amounts shown would represent the real value of the total reserve scheme pension if the bonuses were sufficient to compensate precisely for price rises.

### Table A

<table>
<thead>
<tr>
<th>Age at entry to Reserve Scheme</th>
<th>Weekly pension for man earning:</th>
<th>Reserve Scheme pension as % of earnings</th>
<th>Age at entry to Reserve Scheme</th>
<th>Weekly pension for woman earning:</th>
<th>Reserve Scheme pension as % of earnings at retirement</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>£10</td>
<td>£20</td>
<td>£30</td>
<td>£42</td>
<td></td>
</tr>
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</tr>
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</tr>
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<td>4.1</td>
<td>8.3</td>
<td>12.4</td>
<td>17.3</td>
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</tbody>
</table>

Notes: (1) The amounts of pension are based on the assumption that contributions on earnings at the levels shown would be paid continuously from the birthday in the first column up to retirement age.

(2) On the death of her husband a widow becomes entitled to half his rate of pension.
### TABLE B
RESERVE SCHEME PENSIONS (PAYABLE IN ADDITION TO BASIC PENSIONS)
(Assuming real earnings rising at 3% per annum)

<table>
<thead>
<tr>
<th>Age at entry to Reserve Scheme</th>
<th>Weekly pension for man whose earnings at entry are: £10</th>
<th>£20</th>
<th>£30</th>
<th>£42</th>
<th>Reserve Scheme pension as % of earnings at retirement</th>
<th>Age at entry to Reserve Scheme</th>
<th>Weekly pension for woman whose earnings at entry are: £10</th>
<th>£20</th>
<th>£30</th>
<th>£42</th>
<th>Reserve Scheme pension as % of earnings at retirement</th>
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<td>£8-5</td>
<td>£12-7</td>
<td>£17-8</td>
<td>14</td>
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</table>

Notes: (1) The amounts of pension are based on the assumption that contributions on earnings at the levels shown, increasing at 3% a year, would be paid continuously from the birthday in the first column up to retirement age.

(2) On the death of her husband a widow becomes entitled to half his rate of pension.

### The Reserve Scheme Fund

75. It is essential to the purpose of the reserve scheme that it should be demonstrably self-supporting. The scheme will therefore be fully funded and will be financed solely by contributions from employers and employees and the income from its investments. There will be no Government subsidy, nor will the reserve scheme fund be available for Governmental use. If there were any element of subsidy from the taxpayer employers well able to run their own schemes would be tempted to use the reserve scheme instead, at the taxpayer's expense. Any risk of the scheme becoming seriously unbalanced will be avoided, not only by the adoption of an age-related benefit structure but also by including a profit-sharing element. This will enable “bonuses” to be added both to the pensions in payment and to the prospective pensions (assessed on the age-related scales) of those who have not yet reached pension age. The “bonuses” will depend in amount on the investment performance of the fund; as well as introducing a degree of protection against price rises, they will serve as a regulator which can be used both to avoid deficits and to distribute surpluses. The pensions will thus be built up from two parts—a fixed element, derived from the age-related scales which the scheme undertakes to provide, and a variable “bonus” element which depends on investment performance.

76. To command confidence that the reserve scheme funds will be kept entirely separate from both the Exchequer and the National Insurance Fund, the responsibility for investing them will be put into the hands of the independent
Board of Management. The Board will also have the duty of deciding periodically, in the light of actuarial advice, what bonuses should be declared. In order to offer a reasonable prospect that the bonuses will be sufficient to maintain the real value of the reserve scheme pensions the Board will need, and be allowed, the same freedom of investment as occupational schemes, extending to equities and property. They will be free to decide their own investment arrangements, subject to certain safeguards. In particular they will be put under a statutory obligation to operate the scheme, and conduct its investments, in such a way as to secure the best pensions for scheme members. A statutory limit will be placed on the proportion of voting shares that the reserve scheme can hold in any one firm. The members of the Board, though appointed in a personal capacity, will be drawn from a wide field and include members with special experience of investment and pension matters as well as members appointed after consultation with representative organisations such as the CBI and the TUC. The Board will be required to publish periodic accounts and actuarial reports so that their performance will be open to public scrutiny.

Membership
77. Membership of the reserve scheme will be compulsory for all employees between age 21 and pension age for any period when they are not covered by a recognised occupational scheme; if a scheme does not gain recognition the employees concerned and their employer would be required to contribute to the reserve scheme. There will be no contribution option for married women; whatever contributions they pay will result in additions to their pension, in exactly the same way as for single women. Employees over 21 who are still under the minimum age of entry to their occupational scheme and those serving a qualifying period will have to contribute to the reserve scheme until they actually enter the occupational scheme. Thus the membership of the reserve scheme, consisting essentially of those who are not at the time in an occupational scheme will be different from that of most occupational schemes. Some employees may stay in the reserve scheme for all, or most of, their working life but, more typically perhaps, people will pay contributions to the reserve scheme only for short periods or intermittently, while they are in jobs without pension cover or while they are waiting to qualify for membership of an occupational scheme.

The self-employed
78. Because of the difficulty of collecting earnings-related contributions from the self-employed (see paragraph 43 above), they cannot be included in the reserve scheme. Nor would it necessarily be desirable to make provision of this sort for them, even if it were practicable. The occupational pension of the self-employed person depends on his own initiative: he is in a different position in this respect from the employee who, however active his interest in pension matters, is dependent on the initiative of the employer. For the self-employed, the recently announced changes in the Inland Revenue rules affecting their personal retirement and widowhood provision are of particular significance. These changes allow an increase in the percentage of income before tax which can be paid towards an annuity contract—from 10 per cent to 15 per cent—and permit a tax-free lump sum to be taken in partial commutation of the annuity. Finally, out of the new 15 per cent contribution, up to 5 per cent of earnings may be put towards a widow’s annuity, with the same tax relief as the pensioner’s own retirement annuity.
CHAPTER 3

Finance and Administration

Financial implications

79. The basic scheme will, like the present national insurance scheme, be financed on the pay-as-you-go principle. Its income will be derived mainly from contributions from insured persons and employers; this will be supplemented by the Exchequer contribution and to a small extent by the interest on the reserves, substantially those taken over from the present scheme. Contributions will be set at a level necessary to meet current expenditure. The total level proposed for employed persons is 12.5 per cent of reckonable earnings; this includes the contribution for industrial injuries benefits, and also about 1 per cent for the national health service contribution, both intended to produce broadly the same amount in relation to earnings as the present flat-rate contribution. In addition employers will pay a Redundancy Fund contribution in the region of one quarter per cent.

80. The change to wholly earnings-related contributions for employees and partly earnings-related contributions for the self-employed will greatly improve the buoyancy of the contribution income, and in general it should not then be necessary to increase the percentage of earnings-related contributions when benefits are increased from time to time in accordance with the Government's proposals. Indeed, as explained in the Government Actuary's memorandum (Appendix 3), the contributions necessary for a given level of benefit would on the pay-as-you-go basis be significantly lower by the end of the century than at the outset of the scheme. It is not the intention of the Government to suggest that the basic scheme should in fact accumulate large surpluses in the later years of the century.

81. The Exchequer supplement to the basic scheme will be 18 per cent of the contribution income. This is about the same as is produced by the present arrangements, but the new feature is that it will rise automatically as contributions rise with earnings.

82. The reserve scheme will be financed on an entirely different basis. It will be designed to give a purely actuarial return on the money contributed and will contain no element of Government subsidy. This means that it must be funded along the lines normally adopted for private superannuation schemes. It is not possible to make any firm prediction of the total number of contributors to the reserve scheme but if initially this were in the region of 7 million (about half of them women) the scheme's contribution income, on the basis of current earnings levels, might be of the order of £250 million a year. Taking into account the scheme's outgo and the investment income, and making some allowance for the number of contributors to fall as occupational cover grows, then, in present-day terms, the fund might have built up to something of the order of £5,000 million by the end of the century (or to, say, something like a quarter of the value of all other occupational scheme funds at that time).
83. The Government are confident that the financial arrangements they propose for the reconstruction of national insurance will do away with the constant adjustments of the main rates of contributions which have been a feature of the last twenty years, as well as providing earnings-related pensions for those who for one reason or another cannot be covered or fully covered by the expanding occupational pensions movement.

Manpower implications
84. There will be operational advantage for employers as well as Government Departments in the new arrangements, mainly through changing from a dual system of flat-rate stamped cards and graduated contributions to a single system of fully earnings-related contributions for employers and employees collected through PAYE. In the public service the changeover will lead to a temporary increase in staff to prepare for the new basic and reserve schemes while the present arrangements are being wound up. The full extent of the manpower savings will be achieved some three to four years after the start of the new schemes.

Conclusion
85. Social security is not the exclusive responsibility of the Government. Individuals and employers are deeply involved. Plans for the future of social security are plans for the sort of people we want to be and the sort of society we want to live in. The central issue is the need for a constructive and durable partnership between the State scheme and occupational pension schemes which leaves both free to develop towards objectives that people clearly recognise and freely accept.

86. Only the State scheme can meet the massive obligations that the present generation of working people owe to the present generation of people who have retired from work or are otherwise unable to provide for themselves. The new State basic scheme is designed to ensure that these obligations are met fairly and squarely. Beyond this basic provision there is a special obligation to those members of our society who are particularly hard-hit, the very old, the widows, the chronic sick and the disabled. This again is an obligation that only the State scheme can meet and it is in this direction that it must develop as quickly as resources will allow.

87. Opportunities for higher earners to secure higher living standards in retirement do not depend upon the State. For people of working age, access to a decent occupational scheme should become a matter of course. Personal savings, buying a house, personal insurance—these are additional ways in which people today can decide to make provision for their retirement. The Government’s aim is to encourage more and more people to take these opportunities. But while the social obligations set out in this White Paper are the responsibility of the State the opportunities are the responsibility of individuals and employers. It is by personal enterprise and foresight, and not by reliance on an ever-widening extension of State commitments, that better living standards for our people in the later years of life will be secured.
CONTRIBUTION TABLES

The tables in this Appendix illustrate, as at September 1971, the contributions which would be payable under the new scheme at various earnings levels by comparison with those payable under the present scheme. These comparisons do not, however, indicate the amount of the differences that will actually occur at the start of the new scheme since these will be affected by changes in the levels of contributions needed to finance increases in benefit rates between September 1971 and April 1975.

Notes
(1) The proportion of employed men earning more than £30 a week is about 60 per cent; the corresponding figure for women is about 5 per cent.
(2) It is likely that most employees at the higher earnings levels will be members of recognised occupational schemes and will so be exempt from reserve scheme contributions.
EMPLOYED PERSONS

Table 1

Contracted out at present; exempt from reserve scheme

<table>
<thead>
<tr>
<th>Weekly earnings £</th>
<th>Present scheme</th>
<th>New basic scheme</th>
<th>Comparison £p</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Contribution £p</td>
<td>% of earnings</td>
<td>£p</td>
</tr>
<tr>
<td>Men</td>
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<td>42</td>
<td>1·91</td>
<td>4·55</td>
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Table 2

Not contracted out at present; exempt from reserve scheme

<table>
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<th>Weekly earnings £</th>
<th>Present Scheme</th>
<th>New Basic</th>
<th>Comparison £p</th>
</tr>
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<td>Contribution £p</td>
<td>% of earnings</td>
<td>£p</td>
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28
### Table 3

*Not contracted out at present; member of reserve scheme*

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<th>Weekly earnings £</th>
<th>Present schemes</th>
<th>New basic and reserve scheme</th>
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<td>Contribution £p</td>
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<td><strong>Women</strong></td>
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### Table 4

**Self-employed persons**

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<th>Comparison £p</th>
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<td>% of earnings £p</td>
<td>Contribution £p</td>
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<td>1·25</td>
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PRESERVATION OF OCCUPATIONAL PENSION RIGHTS

General
1. The aim of making legislative provision for the preservation of occupational pension rights will be to ensure that, subject to certain qualifying conditions, an employee who leaves pensionable employment before reaching the pension age of the scheme to which he has belonged should be entitled, from that age, to whatever pension he has earned by his service. The new requirements will be satisfied if a deferred pension is provided for the employee in the scheme he is leaving, but there will be no bar to his acceptance of any alternative the scheme offers which has the effect of maintaining his pension cover. In some cases a transfer to another scheme will be arranged and in others a deferred annuity will be purchased.

2. In general, schemes will have to ensure that deferred pensioners are treated no less favourably in relation to their period of pensionable service than employees who stay on until pension age. In particular, deferred pensions will normally fall to be calculated in accordance with the scheme’s own accrual rules for full-term pensions. The standards prescribed in the legislation will not however prevent schemes from adopting more generous arrangements where they wish to do so, eg some may provide easier qualifying conditions and some may find it convenient to round upwards fractional periods of service or amounts of pension.

SCOPE OF THE LEGISLATION

Pension schemes affected
3. All occupational pension schemes, whether or not they are recognised for purposes of exemption from the reserve scheme, will be within the scope of the preservation requirement. In this context, the term “occupational pension scheme” is intended to cover any scheme or arrangements providing retirement or death benefits for people employed in a particular employment or their dependants, provided that the employer contributes at least part of the cost and the members have an enforceable right to the benefits. Crown and analogous employments will not as such be excluded though the legislation will not bite on the present schemes for members of the civil service and armed forces since these schemes do not enable their members to enforce their title to benefits. The Government will, however, ensure that members of the civil service scheme are treated no less favourably than employees whose schemes come within the scope of the legislation. In normal circumstances, this will also apply to members of the armed forces schemes; but the armed forces, in view of their unique conditions of employment, will need to retain powers to abate or suspend or apply forfeiture to pensions in appropriate cases.

Benefits to be preserved
4. The preservation requirement will apply to whatever benefits would have been available to the member if he had reached the scheme’s normal pension age at the date on which he left the employer’s service. Such benefits may include (a) a member’s personal retirement benefits including any lump sum; (b) benefits payable on his death after retirement, including widow’s pension and guaranteed minimum retirement pension payments; (c) any options to be exercised at the point of retirement, eg commutation of pension for a lump sum, allocation of pension to a dependant; and (d) any contractual provision for increases of pensions in payment.

5. The question whether benefits payable on a member’s death in service should be subject to preservation, ie whether any such benefit must continue to be available in the event of his death after leaving the scheme but before reaching pension age, presents particular difficulties. Such benefits are commonly provided in two quite different forms, a lump sum unrelated to length of service, or a widowhood pension (or lump sum) accruing integrally with other scheme benefits. Benefits of the first type do not readily lend themselves to preservation, and, while preservation of the second type of benefits does not present the same problems, it would not seem right to lay unequal...
burdens on different pension schemes according to more or less fortuitous differences in the type of benefits they provide.

6. On the other hand, if death in service benefits are not made subject to preservation, the wife of a scheme member could be assured of occupational cover in the event of his death either while in the employment or after pension age, and yet have no entitlement to benefit in respect of his years of service in that employment if he dies after leaving the employment but before pension age. The question whether there is any satisfactory means of narrowing or closing this 'gap' will need further study.

Widows and other dependants

7. Occupational schemes which provide benefits for the widow (or other dependent) of a pensioner commonly restrict such provision to a widow married to (or person dependent on) the pensioner at the point when he retired. The question arises whether any such test of marriage or dependancy which is applied to a deferred pensioner should relate to the point at which he reaches retirement age or the point at which he leaves the scheme. In general, it would seem right to allow schemes which provide such benefits to limit their liability to the widow married to (or person dependent on) the member at the time he leaves the scheme—otherwise they would be required to take on a contingent liability they might find no satisfactory means of providing for. But a scheme which provides benefits for the widow of a full-term pensioner even where the marriage took place after the husband’s retirement should be required to give no less favourable treatment to the widow of a deferred pensioner in similar circumstances.

QUALIFYING CONDITIONS

8. The requirement on a scheme to preserve a member’s pension rights will arise if he leaves after the operative date of the legislation and has satisfied the minimum qualifying conditions, namely the attainment of age 26 and completion of 5 years’ pensionable service. The proposed age qualification is linked with the minimum age of 21 proposed for entry into the State reserve scheme and ensures that any one with at least 5 years’ pensionable service after that age will satisfy the qualifying conditions for a preserved pension. For satisfaction of the service qualification, any service will count which the leaving member had built up towards pension in the scheme either before or after the operative date of the legislation, subject to the exclusion of notional, deemed or credited service. Where, however, a person is concurrently a member of more than one scheme in respect of the same employment, then if he has qualified for preservation in one scheme he will be deemed to have qualified in all.

Service before and after operative date: treatment of contribution refunds

9. Where a member leaves a pension scheme after the operative date of the legislation, has attained age 26 and has 5 or more years’ pensionable service, he will be entitled to a preserved pension in respect of the whole of that service, irrespective of whether it occurred before or after the operative date. If such a member has five years or more service after the operative date, a contributory scheme will no longer be permitted to offer him—as an alternative to preserving his pension—a refund of contributions which he has paid since the operative date. This restriction on refunds will not extend to contributions in respect of service before the operative date, nor will it apply to contributions relating to a period of service after the operative date which has lasted for less than five years; in these cases a refund of contributions will still be permitted. In brief therefore a leaving member who satisfies the qualifying conditions may if he wishes have a preserved pension in respect of all his pensionable service; and must have a preserved pension (or otherwise have his pension cover maintained) in respect of all periods of service lasting for 5 years or more after the operative date.

10. Recognised schemes. Although, as explained above, schemes will not be required to preserve pensions for members who leave with less than 5 years’ pensionable service, the employer of anyone who was in a recognised scheme and who does not have his pension rights preserved or otherwise protected will be required to pay to the reserve scheme the contributions which would have been due but for exemption. Any refund of occupational scheme contributions due to the employee may be reduced by his share of the payment to the reserve scheme.
11. In certain types of scheme, however, a different basis of calculation is needed; these include (a) schemes with accrual rules which are weighted in favour of older members or members with long service; and (b) fixed benefit schemes (such as schemes which provide a flat rate pension or a fixed proportion of final salary regardless of length of service). These two types of scheme, along with any others for which the “scheme rules” approach can be shown to be inappropriate, will normally be required to provide the leaving employee with a deferred pension based on “uniform accrual”. That is, they will have to ensure that the preserved pension is not less than the product of the formula \( \frac{A}{B} \times C \), where \( A \) is the period of the member’s actual pensionable service; \( B \) is the period of the member’s potential pensionable service if he had remained in the scheme to the normal pension age (or—in the case of schemes of type (a) above—the age at which he would have earned the maximum permitted pension under the scheme’s rules, whichever is the sooner); and \( C \) is the member’s prospective full-time pension calculated according to the scheme’s own rules, (and based, in the case of a final salary scheme, on his salary at the time of leaving).

12. A few schemes may find special difficulty in applying the method of calculation required by the legislation; and the Occupational Pensions Board will have discretion to approve such variations in the requirements as they may consider appropriate, where they are satisfied that it would not be reasonably practicable to require exact compliance, having regard to the structure of the particular scheme.

**Treatment of credits**

13. Credits may be defined as pension rights in a scheme acquired otherwise than by virtue of actual pensionable service in that scheme. They fall into two broad categories: “given credits” awarded and financed entirely by the employer; and “purchased credits”, purchased by a payment into the scheme at the expense of the member or a previous employer (often on transfer from another scheme).

14. **Given credits.** Where a credit has been given by the employer entirely at his own expense it will have to be preserved (subject to the member satisfying the qualifying conditions for preservation) on the basis of “uniform accrual”, ie the scheme will be required to preserve that proportion of the credit which the member may be deemed to have earned by his actual service, on the assumption that he would have become entitled to the full amount of the credit on reaching the scheme’s pension age.

15. **Purchased credits.** Where a member or previous employer has purchased a credit (or contributed to the purchase of a credit) by a payment into the scheme, it will have to be preserved in full subject to the member qualifying for preservation by virtue either of his service in that scheme or (where the credit was purchased by a transfer payment from another scheme) by his service in the ceding scheme. Where the member arranges to purchase credits by means of payments spread over a period, and leaves before the end of that period, the credits to be preserved will be proportionate to the payments he has made up to the time of leaving.

**Enhanced service**

16. Enhanced pension awarded in respect of particularly arduous service, e.g. in the tropics, is an integral part of the employee’s pension expectation under the scheme’s own rules and will, therefore, have to be preserved in full. But only actual service, as distinct from enhanced or notional service, will count towards the 5 year qualifying condition for preservation.

**INCREASES OF DEFERRED PENSIONS**

**Increase after retirement**

17. Where a scheme makes contractual provision for increasing full-time pensions in payment, it will be required to make the same provision for deferred pensions in payment, so that the deferred pensioner is not put at an unfair disadvantage. Where, however, provision for such increases is at the employer’s or scheme’s discretion it would not seem right to impose a similar requirement since this could have the effect of
CALCULATION OF ACCRUED PENSION RIGHTS

10A. In the interests both of those who run schemes and of their members, the basis for calculating the preserved pension should be as simple as possible, but it must ensure that the early leaver has preserved for him a fair proportion of the pension he would have received if he had stayed to pension age. In the normal final salary, average salary, graded schedule or money-purchase type of scheme the amount of pension or other benefit which has to be preserved will be that to which the member would have been entitled if he had reached the scheme's normal pension age at the date on which he left the employer's service, calculated according to the scheme's own accrual rules for full-term pensioners. Thus the pension to be preserved will be, in a final salary scheme, the accrued fraction of the member's leaving salary; in an average salary, graded schedule or money purchase scheme, it will be the total of the "bricks" (i.e., the periodically accruing amounts) of pension he has earned during his service.

14. Given credits. Where a credit has been given by the employer entirely at his own expense it will have to be preserved (subject to the member satisfying the qualifying conditions for preservation) on the basis of "uniform accrual", i.e., the scheme will be required to preserve that proportion of the credit which the member may be deemed to have earned by his actual service, on the assumption that he would have become entitled to the full amount of the credit on reaching the scheme's pension age.

15. Purchased credits. Where a member or previous employer has purchased a credit (or contributed to the purchase of a credit) by a payment into the scheme, it will have to be preserved in full subject to the member qualifying for preservation by virtue of his service in that scheme or (where the credit was purchased by a transfer payment from another scheme) by his service in the ceding scheme. Where the member arranges to purchase credits by means of payments spread over a period, and leaves before the end of that period, the credits to be preserved will be proportionate to the payments he has made up to the time of leaving.

16. Enhanced service

Enhanced pension awarded in respect of particularly arduous service, e.g., in the tropics, is an integral part of the employee's pension expectation under the scheme's own rules and will, therefore, have to be preserved in full. But only actual service, as distinct from enhanced or notional service, will count towards the 5-year qualifying condition for preservation.

INCREASES OF DEFERRED PENSIONS

Increase after retirement

17. Where a scheme makes contractual provision for increasing full-time pensions in payment, it will be required to make the same provision for deferred pensions in payment, so that the deferred pensioner is not put at an unfair disadvantage. Where, however, provision for such increases is at the employer's or scheme's discretion it would not seem right to impose a similar requirement since this could have the effect of

FORFEITURE OF PENSION

20. Subject to certain safeguards, it is proposed to allow deferred pension from any member with his employment. The scheme authorities have limited prospects of securing further employment for those who have left before the scheme's pension age. Any other provisions may arise in connection with payment of full-term pensions from an expectation of the age of 60. Schemes which provide for the payment of deferred pension in the event of the member's retirement will have to be preserved in full, subject to the member qualifying for preservation by virtue of his service in the scheme or (where the credit was purchased by a transfer payment from another scheme) by his service in the ceding scheme. Where the member arranges to purchase credits by means of payments spread over a period, and leaves before the end of that period, the credits to be preserved will be proportionate to the payments he has made up to the time of leaving.

Other forfeiture rules

21. Any scheme rule under which payment of deferred pensions is affected by some event occurring after the period in payment so as to affect schemes' pensions in payment in the same way as deferred and full-term pensioners. A scheme rules for forfeiture of a deferred pension in the event of the member or who attempts to assign his pension.

Lien rules

22. Schemes will not be precluded from operating a lien on members' benefits which would otherwise

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limiting an employer's freedom to award special increases to those who needed them most, e.g. full-term pensioners on small pensions.

**Revaluing the pension before retirement**

18. Similarly, where a scheme makes contractual provision for revaluing members' prospective pension rights prior to retirement, the same provision will be required for deferred pension rights in the scheme. Ideally it would be desirable for the real value of all deferred pensions to be maintained over the period between award and payment, but there seems no way of ensuring this that would not have the effect, in some schemes but there seems no way of ensuring this that would not have the effect, in some schemes—e.g. those of the graded schedule or money purchase types—of placing the early leaver at an advantage over the full-term pensioner. Alternatively, a special case could be argued for requiring some provision for revaluation in final salary schemes, on the grounds that the employee's preserved pension (calculated as a fraction of his salary at the time of leaving) for each year of his service is likely to fall short of the full-term pension (calculated as a fraction of his salary at retirement) which he would have received for each of the same years if he had stayed on until pension age. But even this limited requirement could produce anomalies in individual cases, and there might be some risk of it deterring employers from setting up schemes of this type at all.

**PAYABLE AGE FOR DEFERRED PENSION**

19. A pension preserved in accordance with the statutory requirements must come into payment not later than the normal pension age of the occupational scheme; that is the age at which, under the scheme's rules, the member concerned would have become entitled to retire on the full pension appropriate to his years of service had he remained in the scheme (assuming that no special circumstances would have arisen such as early retirement on account of ill-health). An exception to this provision will however be allowed where it would otherwise lead to a deferred pension becoming payable before the age of 60. Schemes which provide full-term pensions from an age earlier than 60 ordinarily do so because of circumstances applicable to full-term pensioners, such as limited prospects of securing further employment, which do not apply in the same way to those who have left before the scheme's pension age. Consideration will be given to any other problems which may arise in connection with schemes providing for the payment of full-term pensions from an exceptionally early age.

**FORFEITURE OF PENSION RIGHTS**

20. Subject to certain safeguards, it is proposed that schemes should be permitted to withhold a deferred pension from any member guilty of grave misconduct in connection with his employment. The scheme authorities will have to be satisfied that forfeiture is reasonable in the particular circumstances of the case, taking into account the availability of alternative remedies and the extent to which they have been, or could reasonably have been, exercised. Furthermore, any scheme which wishes to provide for the forfeiture of deferred pensions in its rules, will have to include a right of appeal against forfeiture to an industrial tribunal. (Under the Industrial Relations Bill, industrial tribunals will also hear appeals against "unfair dismissal", but if an employment has satisfactory arrangements for independent arbitration or adjudication those arrangements may be substituted. In such cases, the alternative arrangements will be permitted similarly to cover appeals against forfeiture of deferred pension rights.)

**Other forfeiture rules**

21. Any scheme rule under which payment of, or entitlement to, a full-term pension is affected by some event occurring after pension age (e.g. imprisonment) can be applied equally to deferred pensions in payment so as to maintain parity of treatment between deferred and full-term pensioners. A scheme will also be permitted to provide in its rules for forfeiture of a deferred pension in the event of the bankruptcy of the member, or if he assigns or attempts to assign his pension.

**Lien rules**

22. Schemes will not be precluded from operating a rule which gives the employer a lien on members' benefits which would otherwise have to be preserved, in respect of
sums due to the employer, subject to certain limitations: (a) if the member disputes the amount due, the employer will not be able to exercise the lien without first obtaining an order or judgment from a competent Court specifying the sum due; and (b) a loan or advance by the employer to the employee will not be recoverable by exercise of a lien. Recovery would be effected by deducting the sum owed by the member from the sum decided actuarially to be needed in the scheme to provide the member in due course with his preserved pension, any residual sum being applied to provide a deferred pension for the member.

ADMINISTRATION OF DEFERRED PENSIONS

23. It will be for pension schemes themselves to decide what will be the best arrangements for informing the early leaver of his pension rights and any options available to him on leaving, and also for providing any supporting documentation. Arrangements will no doubt differ as between schemes, depending on their particular circumstances.

ENFORCEMENT

24. The legislation will place a direct requirement on those responsible for the operation of schemes to see that scheme rules conform with the preservation requirements. Before recognising a scheme for the purposes of exemption from the reserve scheme, the Occupational Pensions Board will ensure that the scheme's rules comply with the preservation requirements. In addition, members of all schemes (whether recognised or not) will have the right to apply to the Board if they consider that there has been any failure to comply. The Board will have power to determine whether the scheme rules comply with the statutory requirements and, if they determine that the rules do not so comply, to secure their amendment. The date from which the amendment takes effect will be a matter for the Board to decide, except that they will not be empowered to fix a date earlier than the operative date of the legislation. In addition, the Board will be available to give informal rulings and advice, at the request of those responsible for schemes, as to whether proposed rules satisfy the requirements.

25. In this way, it should be possible to ensure that scheme rules are put in order so as to confer the necessary contractual rights on the leaving members concerned. Any member dissatisfied with the application of the rules to his case will have the same means of redress as would be available to a full-term pensioner in similar circumstances.

26. The jurisdiction of the Board in regard to schemes' preservation rules will not apply to those public sector schemes which are set out in an Act of Parliament or Regulations or in a non-statutory document for the terms of which a Minister of the Crown is responsible. Ministers of the Crown will, however, have access to the Occupational Pensions Board for advice, and the Government intend that questions arising in regard to preservation shall be determined by the Ministers responsible in accordance with the same principles as those which the Occupational Pensions Board apply in the discharge of their corresponding responsibilities for schemes at large.

OVERSEAS QUESTIONS

Schemes based overseas

27. Schemes based overseas, i.e. set up under a trust deed in another country and managed by trustees or administrators resident in that country, will be outside the scope of the preservation requirement, whether or not some of their members work in Great Britain.

Schemes based in Great Britain

28. Members overseas. Employees (other than those locally recruited overseas) who are working overseas for a British employer, or who are on temporary secondment to an overseas employer, will be within the scope of the preservation requirement so long as they remain members of the British-based scheme.

29. Employer overseas. Where the scheme is British-based and the member is living and working in Great Britain, the right to a preserved pension will not be affected by the employer being resident overseas.
30. **Employer and member overseas.** The preservation legislation will not extend to schemes based in Great Britain where both the employer and the scheme member are resident overseas (except, as mentioned above, for employees on temporary secondment to an overseas employer).

**OPERATIVE DATE**

31. It is proposed to bring in the preservation requirements with effect from the same date as the main structural changes in the State scheme.
APPENDIX 3

Memorandum by the Government Actuary on the finances of the proposed schemes

THE BASIC SCHEME

1. The basic national insurance scheme will continue to be financed on the pay-as-you-go principle and contribution rates will be set at the levels required to produce as nearly as practicable a broad balance of income and outgo. For employed persons, the present system of flat-rate and graduated contributions will be replaced by wholly earnings-related contributions payable at a uniform percentage rate on earnings below an upper limit of about one-and-a-half times national average earnings, so that the income of the scheme will move broadly in step with changes in the general level of earnings. The main benefits will remain as under the present scheme and will be paid at flat rates which will be reviewed every two years and increased by amounts sufficient at least to preserve the purchasing power of the benefits.

2. The finances of a scheme of this nature over a long period ahead can best be illustrated by means of estimates based on the assumption of constant earnings and benefit rates, which, subject to the reservations mentioned in paragraph 6, show the relative progress of income and outgo if benefits as well as contributions were to change in line with earnings. For the purpose of the estimates in this report, benefits have been taken at the rates provided for under the National Insurance Act 1971 with earnings constant at the level assumed for September 1971 when these rates will come into effect.

3. The estimated cost of benefits on this basis is shown in Table 1. The future form of the short-term sickness, unemployment and maternity benefits is still under consideration but, in order to give an indication of the total expenditure under the scheme and the level of contributions likely to be required, estimates for these benefits have been included on the assumption that the total cost would be the same as if the provisions of the present scheme, as amended by the 1971 Act, were to remain unaltered. On Government instructions, a rate of unemployment of 2½% has been assumed.

<table>
<thead>
<tr>
<th>Table 1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Estimated cost of benefits under the basic scheme (on the basis of 1971 Act rates of benefit)</td>
</tr>
<tr>
<td>£ million</td>
</tr>
<tr>
<td>Retirement pensions ...</td>
</tr>
<tr>
<td>Widows' benefits and guardians' allowances</td>
</tr>
<tr>
<td>Unemployment benefits</td>
</tr>
<tr>
<td>Invalidity benefits ...</td>
</tr>
<tr>
<td>Sickness benefits ...</td>
</tr>
<tr>
<td>Maternity benefits ...</td>
</tr>
<tr>
<td>Death grant ... ...</td>
</tr>
<tr>
<td>Total National Insurance benefits ... ...</td>
</tr>
<tr>
<td>Industrial Injuries benefits ... ...</td>
</tr>
<tr>
<td>Total National Insurance and Industrial Injuries benefits ... ...</td>
</tr>
</tbody>
</table>
4. The graduated pensions secured under the present scheme through the payment of graduated contributions will remain fixed in money terms and will not be included in the two-yearly reviews of benefit rates. In presenting estimates in terms of constant earnings and benefits, therefore, allowance must be made for the fact that if earnings and prices rise the cost of these pensions will fall in relation to the cost of other benefits and to the yield of contributions, to an extent depending on the rate of increase in earnings and benefit rates. The amounts included in respect of graduated additions in the estimated cost of retirement pensions shown in the table have been adjusted to take account of this factor on the basis of an assumed long-term average rate of increase in earnings of 6% per annum.

5. Estimates of income and outgo on the basis of a joint employee/employer contribution for national insurance and industrial injuries of 11 1/2% (i.e. a total contribution of 12 1/2% of which 1% has been assumed to be for the national health service) are shown in Table 2. Allowance has been made for contributions from self-employed persons on the basis of a flat-rate contribution of £1.50 a week for men and £1.25 for women, together with an earnings-related contribution of 5% of the part of annual earnings falling in the range £1,000 to £2,000. Exchequer supplements of 18% of contributions from insured persons and employers have been included.

Table 2

<p>| Income and outgo of the basic scheme on the basis of a joint contribution for national insurance and industrial injuries of 11 1/2%, illustrated in terms of 1971 Act benefit rates with earnings constant at the level assumed for September 1971 |
|---|---|---|---|---|---|---|---|</p>
<table>
<thead>
<tr>
<th>Year</th>
<th>Expenditure on benefits</th>
<th>Costs of administration</th>
<th>Transfers to Northern Ireland</th>
<th>Contributions from insured persons and employers</th>
<th>Exchequer supplements</th>
<th>Interest</th>
<th>Excess of income over outgo</th>
</tr>
</thead>
<tbody>
<tr>
<td>1975-76*</td>
<td>3,479</td>
<td>130</td>
<td>27</td>
<td>2,930</td>
<td>527</td>
<td>68</td>
<td>-111</td>
</tr>
<tr>
<td>1976-77</td>
<td>3,512</td>
<td>130</td>
<td>27</td>
<td>3,117</td>
<td>561</td>
<td>68</td>
<td>77</td>
</tr>
<tr>
<td>1980-81</td>
<td>3,604</td>
<td>130</td>
<td>28</td>
<td>3,164</td>
<td>570</td>
<td>68</td>
<td>40</td>
</tr>
<tr>
<td>1985-86</td>
<td>3,656</td>
<td>130</td>
<td>28</td>
<td>3,238</td>
<td>583</td>
<td>68</td>
<td>75</td>
</tr>
<tr>
<td>1990-91</td>
<td>3,699</td>
<td>130</td>
<td>29</td>
<td>3,300</td>
<td>594</td>
<td>68</td>
<td>104</td>
</tr>
<tr>
<td>1995-96</td>
<td>3,698</td>
<td>130</td>
<td>29</td>
<td>3,403</td>
<td>613</td>
<td>68</td>
<td>227</td>
</tr>
<tr>
<td>2000-01</td>
<td>3,704</td>
<td>130</td>
<td>29</td>
<td>3,522</td>
<td>634</td>
<td>68</td>
<td>361</td>
</tr>
<tr>
<td>2005-06</td>
<td>3,745</td>
<td>130</td>
<td>29</td>
<td>3,649</td>
<td>657</td>
<td>68</td>
<td>470</td>
</tr>
</tbody>
</table>

*The estimates for 1975-76 make allowance for the loss of receipts in the first year of the scheme because the increased earnings-related contributions will be collected in arrear with PAYE income tax. The estimated shortfall compared with a full year's receipts at the new rates is £180 million in contributions from insured persons and employers and £32 million in Exchequer supplements.

6. Adjustments have been included in Table 2 to allow for the fact that benefits and contributions would not, in practice, change continuously in step with earnings, as is implied in estimates on the basis of constant earnings and benefit rates; these adjustments have for convenience been made to figures for contributions and Exchequer supplement. Even if benefit rates were adjusted at each review exactly in line with changes in earnings they would remain constant between reviews. Also, although contributions will increase with rising earnings, the changes in yields will not be proportional to the movement in earnings since September 1971 as contributions will be credited to the funds in arrears and the upper limit of earnings on which they are payable will, it is assumed, be adjusted only at two-yearly intervals. The net effect of these factors would be to improve the financial position of the scheme compared
with that shown by estimates based on constant earnings to an extent depending on the rate at which earnings increased; for purposes of illustration, the adjustment in Table 2 has been based on a rate of 6% a year.

7. The interest income included in Table 2 has been kept constant for all future years at the current level under the present national insurance and industrial injuries schemes as, under the pay-as-you-go principles on which the basic scheme is to be financed, it can be assumed that contribution rates would be adjusted from time to time to produce a broad balance between income and outgo.

8. Table 2 shows that, on the assumptions made, a total joint contribution of 12\% (including 1% for the national health service) would produce margins of income over outgo in the basic scheme after the first year. The growing surpluses shown for the years 1985-86 onwards reflect the expected changes in the age structure of the population which would lead to a steady improvement in the ratio of the number of contributors to the number of pensioners, which would in practice make it possible for benefits at a level corresponding to that of September 1971 to be provided for lower rates of contribution. The excess of income over outgo shown for the last year in the table is equivalent to the yield of a joint contribution (including the corresponding Exchequer supplements) of about 1\%.

9. The actual contributions required in practice will, however, depend materially on the amounts of the biennial upratings of benefits in relation to changes in earnings levels. If the increases in benefits, whilst fully preserving their real value, were less than in proportion to changes in earnings, lower rates of contribution would be required.

THE RESERVE SCHEME

10. The reserve scheme will provide earnings-related pensions from age 65 for men or 60 for women, and widows' pensions for employees who are not members of recognised occupational schemes. The joint contributions of employee and employer to the scheme will be 4% of the same range of earnings as basic scheme contributions and the benefits secured by each contributor will be related on an actuarial basis to the contributions paid by him and his employer. The scheme will not be financed on a pay-as-you-go basis but will be fully-funded on the same principles as are generally applied in occupational pension schemes, the contributions being invested until required to meet payments of pension and a substantial fund will be built up.

11. The return on the investment of the contributions is an important factor in determining the benefits which can be granted and will depend on the length of the period over which the contributions remain invested. It follows that the lower the age at which contributions are paid, the higher will be the pensions which can be granted for a given amount of contributions.

12. The membership of the reserve scheme will include not only employees in firms with no occupational scheme, or with schemes of inadequate size, but also, for example, employees who are too young or have insufficient service with an employer to be eligible for membership of his scheme. Movement into or out of the reserve scheme on a change of employment will also be common. It can thus be expected that a substantial proportion of the members will contribute to the scheme for only a few years and may in some cases have two or more short spells of contributing membership.

13. The reserve scheme has been designed so that the amounts of pension provided will give an actuarial return according to the age at which each contribution is paid. It is recognised that this basis of assessing the relationship between contributions and pensions will differ from the practice in most occupational schemes which are normally designed for employees serving an employer throughout their working lifetime. It is not important in such schemes for the return on the employees' contributions to be strictly related to the age at which they are paid or for the employers' contributions to be allocated to individual employees. Moreover, it is usual to have separate schemes for manual workers (whose pay normally remains largely independent of age) and non-manual employees (who in many cases start with relatively low earnings and end with higher pay). None of these features will apply to the reserve scheme. A sub-
stantial proportion of members will contribute for only part of their working lifetime and thousands of different employers will be paying into the same scheme, although each will have his own policy of recruitment, salary progression and promotion and his own pattern of manual and non-manual workers. To avoid an unacceptable degree of inequality of treatment among different employers and among employees with widely differing career patterns in a scheme which cannot look for any Government subsidy whatever the composition of its membership, it is necessary for the terms to take account of the ages at which contributions are paid.

14. Table 3 shows for specimen ages the rates at which pension would be secured in return for contributions paid on the basis of scales considered suitable for this purpose. The scales must be regarded as provisional as full details of the scheme have not yet been finally settled.

<table>
<thead>
<tr>
<th>Age last birthday at end of tax year</th>
<th>Pension for £10 contribution (p per week)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Men</td>
</tr>
<tr>
<td>21</td>
<td>9.0</td>
</tr>
<tr>
<td>25</td>
<td>7.7</td>
</tr>
<tr>
<td>30</td>
<td>6.4</td>
</tr>
<tr>
<td>35</td>
<td>5.3</td>
</tr>
<tr>
<td>40</td>
<td>4.4</td>
</tr>
<tr>
<td>45</td>
<td>3.7</td>
</tr>
<tr>
<td>50</td>
<td>3.1</td>
</tr>
<tr>
<td>55</td>
<td>2.5</td>
</tr>
<tr>
<td>60</td>
<td>2.1</td>
</tr>
</tbody>
</table>

15. The scales for men include provision for widows’ pensions of one half of the husband’s pension or, in the event of death before retirement, one half of the prospective pension secured by contributions paid up to the time of his death. The lower benefits for women are attributable to the earlier retirement age and greater longevity, the effects of which more than offset the provision for the cost of widows’ benefits allowed for in the scale for men.

16. The benefit scales shown in Table 3 have been calculated on the basis of a rate of interest of 4% per annum. The rates of mortality assumed have been derived from the experience of the general population over recent years with allowance for future improvement on the basis of the trends over the last fifty years. It has been assumed provisionally that 5% of contribution income will be required for expenses, including the amounts which must be set aside to meet the future costs of paying the pensions.

17. The Board of Management will have wide powers of investment and it is to be expected that the return obtained on the investments will exceed the rate of 4% on which the benefit scales are based. Actuarial reviews of the financial position of the scheme will be made at regular intervals and investment earnings in excess of 4% can be expected to result in a surplus of assets over liabilities being revealed at such investigations. These would enable the Board to declare bonus additions both to pensions in payment and to the prospective pensions of persons not yet retired, and
over the years these bonuses might be expected to offset, or offset to a substantial extent, the effect of rising prices on the purchasing power of the pensions. It must be emphasised, however, that this cannot be guaranteed because the level of bonuses must depend on the net amounts of the profits emerging as a result of deviations between the actual experience and the assumptions underlying the benefit scales in regard to factors such as interest, mortality and costs of administration. A profit-sharing basis of this sort is the only satisfactory arrangement for a scheme which is to be fully self-supporting with no possibility of Government subsidy.

18. It may be necessary from time to time to revise the benefit scales to take account of any substantial variations from the assumptions regarding mortality or other factors in order to preserve suitable margins in the scales and to maintain equity between contributors at different times and at different ages. It is to be expected, however, that changes in the scales will be required only infrequently and these would apply only to contributions paid after the date of the change; benefits secured by earlier contributions would be unaffected.

19. At the commencement of the scheme about 18 million employees would have to be covered either by recognised occupational schemes or by the reserve scheme. The number covered by existing schemes may currently by in the region of 12 million, but not all occupational schemes at present provide benefits at the minimum level required to qualify for recognition. Also, the total of 12 million includes some persons outside the age limits for reserve scheme membership. If it is assumed that nearly all employers with schemes satisfying the requirements for recognition will seek exemption from the reserve scheme, that other schemes will be improved to bring them up to the necessary standard and that new schemes will be set up, then the numbers in the reserve scheme might initially be in the region of 7 million, but this estimate must be regarded as highly conjectural.

20. With a total membership of 7 million, of whom about a half might be women, contributions to the scheme on the basis of current earnings levels might be of the order of £250 million a year, of which nearly £100 million would be paid by employees and the balance by employers. At first, almost the whole of the contribution income will be available for investment, and for a considerable time the interest income will exceed the payments of pension, which will build up slowly over many years. The annual amount available for investment can, therefore, be expected to increase and, even allowing for a reduction in membership of the scheme as a consequence of the growth in occupational pensions, it seems probable that the invested fund will build up by the end of the century to a figure, in present day terms, of the order of £5,000 million.