

Introduction

The **1908 Old Age Pensions Act** introduced the first general old age pension paying a non-contributory amount of between 10p and 25p a week, from age 70, on a means-tested basis from 1 January 1909.

The **1946 National Insurance Act** introduced a contributory State pension for all. Initially pensions were £1.30 a week for a single person and £2.10 for a married couple, paid from age 65 for men and 60 for women, effective from 1948.

One of our major challenges as financial planners is to convince clients who have yet to retire that most of them **need to move their pension planning into a higher gear**. Those who are relying mainly on the State to provide for them in retirement will, as ever, be very disappointed with this important phase in their lives.

"Anyone who retires solely on the Basic State Retirement Pension and makes no other provision will, as has always been the case, retire in abject poverty."
Jeff Rooker, Minister of State
Department of Social Security 29.11.1999

The majority of our clients are generally not in this position and have a combination of **occupational pension scheme benefits, private pension benefits and investment income** to provide the bulk of their income in retirement. The State pension benefit is then simply a useful top-up to these.

We would normally encourage clients who are age 55 plus to obtain a **State Retirement Pension Forecast** as part of their pension planning. However, the Government has recently announced that there will be a year's delay to provide these for people retiring on or after 6 April 2010. This is because their computer systems are in the process of being updated to reflect the changes introduced by the Pensions Act 2007.

The State Pension Age

The State Pension Age is 65. This applies to both men and women except that women born before 6 April 1955 have a lower State Pension Age as the following table shows:

Date of Birth		State Pension Age for Females	
From	To	From	To
Before 6 April 1950		60	
Apr 1950	Dec 1950	60 and 1 month	60 and 9 months
Jan 1951	Dec 1951	60 and 10 months	61 and 9 months
Jan 1952	Dec 1952	61 and 10 months	62 and 9 months
Jan 1953	Dec 1953	62 and 10 months	63 and 9 months
Jan 1954	Dec 1954	63 and 10 months	64 and 9 months
Jan 1955	Apr 1955	64 and 10 months	65

There is a simple State Pension Age Calculator at the following website address

www.thepensionservice.gov.uk/resourcecentre/statepensioncalc.asp

The Basic Retirement Pension

There are two retirement pension benefits that can be provided by the State to eligible persons. First there is the **basic retirement pension** (or 'old age' pension).

This is a basic **flat-rate pension** funded on a **pay-as-you-go basis**, which aims to provide a pension of **approximately 20% of national average earnings**.

It is not related to salary but to obtain the maximum pension you must have paid (or have been credited with) national insurance contributions for **about 90% of your expected working life**. This is taken as 49 years although for a female born before 6 October 1954 this is reduced in stages to a minimum of 44 years. The pension is **reduced proportionately** down to 25% of the maximum, for which NI contributions should have been paid or credited for between 10 and 11 years.

For those retiring on 6 April 2010 or later the **qualifying years reduce to 30** for both men and women.

The pension is increased each year in line with the Retail Prices Index (RPI).

An additional payment is made for a married couple **where one of the parties has entitlement to the basic state pension** and the other's earnings are below a set Department of Work and Pensions minimum.

State Second Pension (S2P)

In respect of earnings in excess of the Lower Earnings Limit an employee may also receive a further pension amount from the **State Second Pension** (referred to as **S2P**). This began on 6th April 2002.

It is being introduced in two stages. Initially it is an earnings-related scheme, similar to the State Earnings Related Scheme (SERPS) that it replaced but with three different accrual rates.

The **Pensions Act 2007** put in place proposals to reform the State Second Pension (formerly SERPS - the State Earnings Related Pension Scheme) so that it becomes a **flat rate weekly top-up** to the Basic State Pension by around 2030.

To ensure this timetable is met the Chancellor announced in his Pre Budget Report that State Second Pension flat rate will commence in **2009 rather than 2010**.

The rate of build up of S2P will vary for each tax year depending on the individual's earnings as follows:

Earnings per Year		S2P Accrual
Band 1	Between the Lower Earnings Limit and the Lower Earnings Threshold	40%
Band 2	Between the Lower Earnings Threshold and the Higher Earnings Threshold	10%
Band 3	Between the Higher Earnings Threshold and the Upper Earnings Limit	20%

If you are **self employed** you neither contribute to, nor are you eligible to receive benefits from, S2P (although you will still do so from any periods of employment).

Lower Earnings Limit (LEL) - This is the minimum level of earnings (**£4,680 pa** for 2008/2009) that an employee needs to qualify for contributory social security benefits, such as Retirement Pension.

If an employee's earnings reach or exceed this level, but do not exceed the Earnings Threshold, they will not pay NICs but will be treated as having paid them when claiming benefit.

Upper Earnings Limit (UEL) - Maximum level of earnings on which an employee has to pay full NI contributions. (**£40,810 pa** for 2008/2009). The rate is reduced to 1% above this level. Employers' NI contributions have no limit.

Lower Earnings Threshold (LET) - This threshold is used in the calculation of S2P. For any individual earning between the Lower Earnings Limit and the Lower Earnings Threshold, they will be treated as if they earned the Lower Earnings Threshold (**£13,500 pa** for 2008/2009).

In other words any employee earning between £4,680 pa and £13,500 pa will receive S2P benefits assuming their earnings are £13,500 pa.

Higher Earnings Threshold (HET) - This is another threshold used in the calculation of S2P. This is approximately 3 times LET less 2 times LEL (**£31,100 pa** for 2008/2009).

The State Earnings Related Pension Scheme (SERPS)

SERPS was replaced by S2P on 6th April 2002, having begun in 1978. As governments realised the true cost to them of providing SERPS **its benefits were gradually cut back**.

Under the SERPS scheme **it was possible to receive a pension of up to 20%** of the income that has been earned between the lower and upper earnings limits.

Higher amounts up to **a maximum of 25% of band earnings** are available for those retiring before 2009.

The Graduated Retirement Pension

This was also an earnings related scheme which **preceded SERPS** and operated between 1961 and 1975. It provided additional benefits on top of the basic State Pension.

Every £7.50 contributed by a man and every £9.00 contributed by a woman bought one unit of benefit which is a weekly pension of 10.98 pence (2008/2009).

The maximum Graduated Pension that you can currently receive is £407 a year (or £340 a year for females). From **April 2010 a woman's Graduated Pension will be calculated as for a man's**.

A widow may inherit half her husband's Graduated Pension when she reaches State Pension Age. A widower, on the other hand may only inherit if they had both reached State Pension Age before his wife died.

Contracting Out

Many **employees in occupational pension schemes** are automatically contracted out of S2P and pay reduced National Insurance Contributions. Other employees have decided to **contract out of S2P by means of a personal pension plan**.

You may have contracted out of SERPS prior to 6th April 2002. In this case the contracting out certificate will **automatically be applied to S2P without further paperwork**.

Please refer to our Guide: *Contracting out of the State Second pension (S2P)*.

Taxation

Tax is **never deducted from State Pensions**. Instead the amount paid is aggregated with any other income to establish if there is a tax liability. If there is, then **the other income will bear it**.

Divorce

An individual **may use the contribution record of a divorced spouse** to top-up his or her own entitlement to the Basic State Pension.

Spouse's Benefits on Death

An individual **may use the contribution record of a deceased spouse** to top-up his or her own entitlement to the Basic State Pension.

Deferring Your State Pension

If you choose to claim your State Pension late you can now take **a lump sum payment**, or receive **higher weekly pension payments**. You can choose to defer your State Pension and receive **a one-off taxable lump sum payment** instead of a weekly increase, when you finally claim.

To be eligible for the lump sum option, **you must defer your State Pension for at least 12 consecutive months**. The lump sum will be based on the amount of weekly State Pension you would have received with **an interest rate at 2% above the Bank of England base rate**. If you choose a lump sum, your weekly State Pension will then be paid at the normal rate.

To be eligible for extra weekly State Pension **you must defer your State Pension for at least five weeks**. The weekly pension will **increase by 1% for every five weeks** you do not claim.

There is **no longer a maximum time** that you can put off claiming State Pension.

Overseas Aspects

If you have lived outside the UK for part of your working life you may still be entitled to a Basic State Pension **based on the number of years of your working life in the UK**.

If you lived in a country in the EEC, or any country whose social security system has a reciprocal agreement with the UK, then any social security payments made there, or residence there, **may count towards the requirements for the UK Basic State Pension**.

Your right to the Second State Pension or an earlier earnings related element **does not depend on the right to a Basic State Pension**.

There is no minimum number of qualifying years' contributions as there is for the Basic State Pension, except that the earnings related element is based on complete tax years.

It is also possible to **have a State Pension paid overseas if you retire abroad** and in certain countries you can also receive the annual increase.

You should contact the Pensions Service for details of countries who have agreements allowing such increases.

Pension Credit

The **State Pension Credit** is a means tested social security benefit which commenced on 6 October 2003. The State Pension credit **aims to provide people aged 60 and over with a minimum level of income** and to give some extra help to people aged 65 and over who have modest incomes above the minimum guarantee and who have made savings for their retirement.

The State Pension Credit replaces the income support (minimum income guarantee) for people aged 60 and over. The State Pension Credit also includes **a new type of assistance, called savings credit**, for people aged 65 and over. The credit consists of two elements, the Guarantee Credit and the Savings Credit.

- **Guarantee Credit** - This is generally available for claimants **aged 60 or over** (in the case of a couple only the eldest person must be 60 or over) who are resident in Great Britain and are not subject to immigration control.

The Guarantee Credit will raise the claimant's income to the level of the appropriate minimum guarantee which for a single person is currently **£124.05 a week** and for a couple **£189.35 a week**.

In this context a 'couple' includes someone who has a husband, wife or civil partner, or they live with a person as if they were married to them or as if they were in a civil partnership with them.

- **Savings Credit** - This is generally available for claimants **aged 65 or over** (in the case of a couple only the eldest person must be 65 or over).

The amount of savings credit depends on how much a claimant's 'qualifying income' exceeds the savings credit threshold. The **maximum savings credit** payable per week for a single person is currently **£19.71 a week** and for a couple is **£26.13 a week**.

To obtain savings credit your **qualifying income must be no more than £173.33 a week** if you are single or **£254.68 a week** if you have a partner.

For further information see our Guide: *State Pensions Credit*.

Further information

For further background information on State Benefits you should visit:

www.direct.gov.uk

www.dwp.gov.uk

www.thepensionservice.gov.uk

Please note that **this information does not constitute personal advice** and should not be treated as a substitute for specific advice based on your circumstances. Information relating to Social Security benefits is based on our understanding of legislation and practice in force at the date of this Guide. Whilst we believe our interpretation of current benefits and practice to be correct in these areas, we cannot be responsible for the effects of any future change in interpretation or treatment.

In particular you are warned that State Benefits are subject to alteration and, in any case, the value of such benefits may depend on an individual's circumstances.

For personal advice

If you would like to discuss your pension provision or receive a review of your existing pension plans, please ask your usual Arch adviser or contact us via one of the following:

Tel: **0845 3700 661**

Email: **enquiries@arch-fp.co.uk**

Online: **www.arch-fp.co.uk**