

British
Chambers of
Commerce
The Ultimate Business Network

Pensions and the Ageing Society Policy Brief

Updated: December 2009

Demographic change will be one of the biggest issues facing the economy in the next century. Business believes changes to pension provision are necessary if the UK is to meet this challenge.

Background

The UK population is changing. In 2008, a 65 year old man could expect to live for another 20.8 years, but by 2050, this figure will have risen to 25 years. At the same time, the number of people of working age is also declining. In 2008, the working age/pensionable age ratio was 3.23 but in 2033, this will have reduced to 2.78. This should be compared to further back in history. In 1901, there were 10 people of working age to each pensioner¹.

Thanks to demographic change and rising costs, pension provision is an increasingly important issue. In particular, the current level of public sector pensions has become unsustainable. Many public sector workers make no contribution to their pension at all, yet are still entitled to a very generous Defined Benefit (DB) scheme on retirement. DB schemes are dead in the private sector, no new schemes are opening and existing schemes are shutting to new members, or shutting down completely. Given tight public finances, and the sacrifices companies and employees have had to make on their own pension schemes, business believes that it is crucial to revisit the affordability of public sector pensions and to develop a more sustainable model.

The changing pensions landscape also gives rise to other issues for the business community including:

- The Default Retirement Age (DRA);
- The future of Defined Benefit (DB) provision; and
- Compulsory employer pension contributions from 2012.

The Default Retirement Age

Summary

The Default Retirement Age (DRA) allows employers to legally dismiss employees aged 65, as long as they have been informed of their right to request to continue working. Employers may also, if it is a proportionate means of achieving a legitimate aim, set the retirement age in their business earlier than 65.

The DRA was challenged in the recent 'Heyday' case, which tested whether it was incompatible with EU law. This ruling found that the DRA was legal. However, the judge commented that one of the reasons for this decision was that the Government had already committed to undertake a review of the DRA. He also questioned whether, if the DRA was being legislated for today, he would have made the same decision.

Government Policy

The Government has recently brought forward a review of the DRA, indicating that they believe some change is necessary.

Opposition Policy

The Conservatives have committed to increasing the pension age to 66 from 2016, implicitly suggesting that the DRA would also have to rise to 66. However, they have not made a firm commitment to keeping the DRA.

The Liberal Democrats have called for the DRA to be scrapped as soon as possible. They are pushing for an amendment to be tabled to the Equality Bill, due to be implemented in 2010.

¹ Department for Work and Pensions (DWP)

BCC Position

The British Chambers of Commerce supports the DRA as a useful legal tool for businesses and as a trigger for a discussion regarding an employee's future with the company. We recognise some changes need to be made and support the Government's review.

However, 65 may not be the right age for the DRA. In a changing society where many people will wish to, and need to, work longer, it does not make sense to force productive members of society out of work. The DRA should mirror the proposed changes to the state pension age² to prevent a 'gap' emerging where some people can no longer stay in work and also are not entitled to state support.

The Future of Defined Benefit (DB) Provision

Summary

Membership of DB schemes in the private sector continues to decline. In 2008, 50% of schemes were closed to new members, compared to 45% in 2007. Nearly a third of schemes are sponsored by manufacturing employers.

In 2004, the Government established the Pensions Protection Fund (PPF) to provide compensation to employees whose sponsoring employer becomes insolvent. In order to fund this compensation, the PPF levies a charge on all private sector DB schemes.

As the total number of schemes has declined, the number of schemes that have found themselves in difficulty has increased. This has meant the PPF is in the position of paying out more benefits to employees whilst having fewer schemes that pay into the PPF levy.

Chamber members consistently report that the levy is too high, too complex to understand, and too unpredictable³.

Government Policy

The Government created the PPF in 2004, largely as a reaction to public anger after Robert Maxwell stole £400m from his company's pension fund. They have so far resisted calls to make wholesale reforms to the PPF by part-funding the levy themselves, or by guaranteeing that the Government will be the lender of last resort to the scheme.

Opposition Policy

The Liberal Democrats are concerned that the PPF and the levy are unsustainable in the longer term and have called on the Government to be a guarantor of last resort.

BCC Position

The Private sector DB provision will continue to decline in the UK and this means that the current method of funding the PPF is unsustainable, although we agree that compensation must be available to employees whose pension savings are at risk.

BCC produced a report in August 2009 detailing a number of recommendations regarding the PPF and the levy, including:

- The suspension of the levy for 2010/11;
- Redistribution of the burden so that the worst performing schemes no longer pay the highest premiums;
- The amount collected each year must be brought back down to £300m, which would increase both the affordability and predictability of the levy; and
- Dun & Bradstreet (the source of business information used by the PPF) should make their insolvency calculations more transparent and give employers the right to properly analyse their score and the components behind it.

² The pension age is due to rise, for men and women, to 66 in 2024, 67 in 2034 and 68 in 2044. Each rise will be phased in over two years.

³ BCC Report 'Contributing to Economic Recovery: Reforming the PPF Levy' August 2009



2012 Pensions Reform

Summary

The Pensions Act 2008 legislated for a new type of pension provision in the UK which involves a compulsory contribution for employers and employees, as well as tax relief. The minimum contributions are split as follows:

- Employees 4%
- Employers 3%
- Tax relief 1%

Although all employees will have to be automatically enrolled into a pension scheme, they do have the opportunity to opt out. If they opt out within a specified period of time then they will be entitled to a refund of any contributions; they also have the right to opt back in at any time. Every three years, all employees must be re-enrolled and must opt out again if they wish.

Employers have a wide range of obligations under this legislation, aside from making the contribution. They must register their pension scheme, enrol all their employees, provide all their employees with information about the scheme, accept and check opt-out forms and process payments.

These reforms will begin in October 2012, but it will take three years for all employers to be subject to the new obligations. The current proposals are that employers will be split into 30 tranches, depending on their PAYE number. The larger employers will be subject to the duty first. Any new business that starts up and begins employing people between October 2012 and October 2015 will begin their contributions at the end of the three year lead-in time, whatever the size of their PAYE number.

Alongside the reforms, the Government has set up the Personal Accounts Delivery Authority (PADA) to implement a scheme with a public service obligation to accept any employer who wishes to use it. This is to ensure that all businesses will be able

to meet their obligations under these reforms, as there was a concern that current pensions providers may not think it economical to provide a scheme to meet the needs of micro businesses and very low earners.

Opposition Policy

There was cross party support for the thrust of these reforms and the idea of automatic enrolment. The Conservatives have stated that they will reconsider whether PADA is necessary should they win the next election. They have also expressed some concern over the administrative burden of the scheme on employers.

The Liberal Democrats also support the scheme but say that their priority is to increase the basic state pension. This, they argue, is the best way to help ensure low earners have a decent retirement.


BCC Position

Pension saving in the UK is too low, resulting in a high degree of dependency on the state. The poor state of the public finances has compounded this problem. BCC fully accepts that the Government must encourage people to save more.

Businesses are already having to provide a 3% contribution, and in return for this, the administrative burden that falls on them should be kept to the absolute minimum. However, under the current plans, we do not believe this is the case.

Government's impact assessment, which suggests a £200 per year administrative cost for SMEs, is woefully inadequate. Businesses that have never offered a pension scheme before are likely to require some help and advice to even choose a scheme for their staff. This is likely to cost over the £200 estimate alone, without the ongoing running costs, and potential new software required.



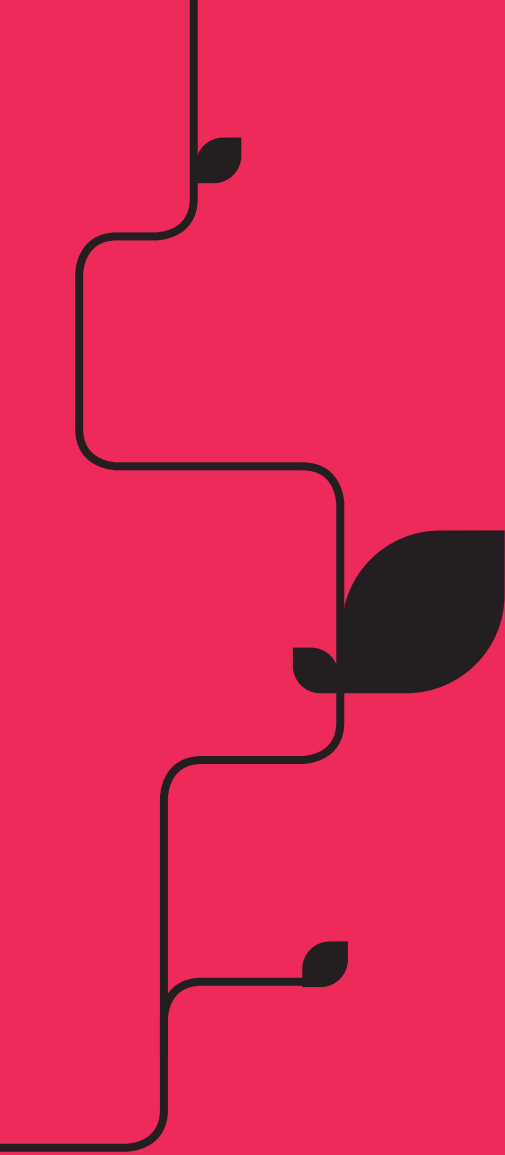


The Government has a real communications issue here. The Pensions Regulator (TPR) has been charged with ensuring compliance, but to most SMEs they will be an unfamiliar body. The long lead-in period of three years compounds the communications difficulties, as does the complexity of the reforms.

We are calling on the Government to simplify these reforms, placing more of the administrative burden on schemes. Examples would be to remove the requirements for businesses to distribute information to their employees, to check that the opt-out form has been correctly filled in, to process refunds and to update the scheme with employees' personal information.

In order for the three year lead in time to go as smoothly as possible, there should be a much lower number of tranches than 30. Re-registration and re-enrolment currently have to take place every three years from the point at which the employer became subject to the duty. This must be changed to common commencement dates in either April or October each year.





Applicability

UK wide.

Contacts

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