

## Choice and Risk in Pensions – Contracting Out in the UK

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### Abstract

The aim of this paper is to identify, trace and analyse the policy trends of various governments towards welfare provision, and in particular to the provision of pensions for its citizens, through the concept of contracting out of the state pension provision. This will be undertaken by examining six periods which have been divided according to the ruling government of the day, namely, the pre-contracting out era (which is of course largely ignored); the genesis years for contracting out; the years of the Castle reforms; the era of popular capitalism; the years of New Labour and the Coalition years. Contracting out will be examined against the extant social justice dimension which still survives in UK policy and legislative initiatives. Although contracting out has been abolished by the previous government its effects will be with us for some time to come.

**Keywords:** Social justice, state pensions, re-distributional basis of government policy, occupational and private pensions, contracting out.

### Introduction

Nowhere is the ideological policy and precepts of social justice of a government more clearly and accurately reflected than in the approach it takes to the provision of welfare and, particularly, pensions for its citizens. This covers not only the provision of the state pension, but also the way in which it allows, accommodates and promotes other forms of pension provision, and the interaction between the two. The aim of this paper is to identify, trace and analyse the policy trends of various governments through the mechanics of the concept of ‘contracting out’ of the state pension scheme, and to examine both their intended and unintended policy impacts. Moreover, the paper aims to undertake an analysis of contracting out, identified as a means of state promoted market organisation of pension provision, against the social justice dimension extant in UK policy and legislative pension initiatives. Although latterly, a UK government has succumbed to the call to abolish contracting out, its effects are with us for some time. Moreover, in itself, it is a fascinating microcosm of a pensions/welfare social policy maelstrom over the last sixty or so years.

State pension provision has existed in the UK for 100 years, and during this time six distinct periods can be identified. In the post-1955 period pension provision and contracting

out has been used to reflect different policy objectives, yet there also being identifiable themes pervading all periods. The periods are,

1. 1908-1955, the pre-contracting out era;
2. 1955-1975, the advent of contracting out;
3. 1975-1979, the 'Castle' reforms;
4. 1979-1997, the advent and development of 'popular capitalism'; and
5. 1997-2010, New Labour.
6. 2010-to present, the Coalition.

Given our stated focus upon contracting out we concentrate on periods 2 – 6. The social and political structure of the UK over this period has meant that no government has intended that the British approach to retirement income equates to the more generous levels of state pension payable by some European counterparts. This is not to say that such approaches have not had their advocates, but as we shall see the policy objectives have been largely dominated by the idea that state pension provision is to remove, or at least ameliorate, poverty in old age. Whilst undoubtedly there are today a number of objectives, particularly the encouragement of retirement saving, dealing with poverty is still seen as a significant feature of the retirement pension and associated means-tested benefits. The socialist movement in the UK, most readily identifiable as embracing the virtues associated with social justice and largely finding its governing force through the Labour party, (in both guises of 'Old' and 'New', although the Liberal Democrat aspect of the coalition government similarly embraces such virtues), has never formally committed itself to major policies to attain the levels of taxation and/or redistribution of resources to fund more generous retirement benefits. Conservative governments have likewise never sought to attain pension levels above basic income replacement: they have approached the state pension from a different, though not always an entirely tangential, perspective. Governments have also viewed the state pension (combined with other state benefits for the lowest income brackets) as a mechanism through which redistribution of economic resources to fund pension benefits designed to avoid poverty in old age can take place – though the extent to which this takes place is contentious. One thing is clear though and that is that pension benefits have played, and will continue to play, a major role in social and political thinking.

We shall see that one cannot divorce contracting out from the legislative and policy context in which the major initiatives have developed, because it in itself has been a simple (notwithstanding that it adds to the overall complexity of the British pension system), yet effective part of the mainstay of pensions policy thinking for some 52 years. By this we mean that contracting out has been part of the gradual erosion of the state as major pensions provider in the UK. Though this may not have been a direct or intended motivation when contracting out was established, it has not been an accident. Successive governments over the relevant period have courted the private sector with a number of mixed, if occasionally ill elucidated, and at times, concurrent, policy motives. For example, contracting out has been a tool in an ideological crusade to undermine a putative dependency culture that the welfare state promotes. It has been a vital part of an economic crusade to deal with the burden that public expenditure on the state pension scheme has presented: though the irony in this is that fiscal circumstances have meant that in relation to certain types of private provision, namely the defined contribution schemes (including the Appropriate Personal Pension), advisers are suggesting that members contract back into the state scheme. It has also in part been a contributor to national prosperity by providing for added private pensions investment. These 'positives' have come at a cost to the lower income groups (pensioner and non-pensioner) by questioning the ability of governments to redistribute resources to what are generally the

lowest income groups. This latter point is important given the recognition that ‘justice’ in the context of social justice is not solely concerned with income/resource levels, but we do not deny the importance of resource/income as a facilitator of wider social justice values and attributes. The previous government accepted the recommendations of the Pensions Commission in its second report, that contracting out be abolished for Defined Contribution Schemes, whilst maintaining the mechanism for Defined Benefit Schemes (Pensions Commission, 2005; Pensions Act 2007). It is important to note that in adopting these suggestions, the prime motivation appears to be ‘cost led’.

The unique thing about the UK compared to its major European comparators is that notwithstanding its commitment to providing a state pension through so-called National Insurance (NI) – the reality of this being the ‘pay as you go’ system of funding - it has relied upon and fostered the private provision of pensions for the employed and self-employed. Today this has even been the driving force behind pensions saving for those receiving below average, or at least moderate incomes and those with sporadic work patterns with the stakeholder pensions central to the Blair government welfare reforms. This also took hold under the Brown government with the automatic employee enrolment in employer schemes with the option of a state privatised alternative (set up under the trust mechanism), of ‘personal accounts’, which was a move to counter under-saving in the workforce (Department of Work and Pensions (DWP), 2006a; Pensions Act 2008). Private pensions have been funded by contributions that are invested in, inter alia, stock markets, to provide benefits that are over and above the levels of benefits received under the state scheme. In essence the market provision of pension benefits for large numbers of people in the UK has been accepted in governmental thinking, with seemingly little demur, to be solely capable of providing retirement pensions consonant with, for the employed at least, relative earning capacity and this has certainly been the case for higher income earners. Current trends dictate that this is to be the case for the moderate earner also. Whether this is indeed the case is a moot point given the vagaries of investment performance, but this is beyond the scope of this paper. This has left larger numbers, particularly those with either no, little or sporadic employment to rely on the lower pension and associated welfare benefits paid to avoid poverty under the state scheme. The unusual feature of the UK pensions structure notwithstanding this long reliance upon the market place, is that it still (at least for the present) exhibits communitarian values. All that are eligible in terms of their NI contributions record receive what is termed a basic state pension, with those that are eligible to do so ‘purchasing’ higher benefits over their working lifetime, for example, State Earnings Related Pension Scheme (SERPS) from 1978 – 2002 and State Second Pension (S2P) from April 2002, through additional financial contributions to the state in the form of higher NI payments, or by additional private provision through personal or occupational pensions. The basic state pension is also received in some cases where there is no previous NI contribution record. This public/private provision has a long antecedent history and the private provision of pensions in the UK has fostered immense wealth in pension providers, immense taxation revenue for governments and immense lobbying power among interested providers and participants. It is the latter points in particular that have created the specific focus of this work, namely the mechanism whereby a person can ‘contract out’ of the higher or second element (that is the earnings related element), of the state pension. Though we shall consider the point in more detail below, it is worth pointing out that when contracting out was introduced, the undeniable motivation was that a private or market place pension provision was both successful and desirable. Furthermore, while the state was to provide universal pension benefits with some recognition of the extra purchasing ability (and one could highlight additional expectations in terms of the level of retirement income) of the employed, it has in effect legislated for a competitor in this latter respect. This idea has gained an unusual

political consensus given that it was a Conservative government that introduced the measure. Recent times have seen government thinking in the UK place ever more reliance on the market place as a source of retirement provision, particularly in light of the challenges the state scheme is predicted to face in 20 – 25 year's time.

### **1955- 1975: The Advent of Contracting Out**

The idea of a graduated state pension was first mooted in a Fabian Tract of 1955, *New Pensions for Old*. Abel-Smith and Townsend questioned the provision of a flat rate pension from flat rate contributions. The tract formed the basis of some of the ideas in the Labour policy document, *National Superannuation Labour Policy for Security in Old Age*, 1957. In this document it was suggested that the existing first tier NI should be the basis for a larger earnings-related pension, with two components. Those people who were adequately protected by an occupational scheme could contract out of the state scheme.

The National Insurance Act 1959 introduced the concept of contracting out. It introduced a graduated or earnings related pension (the State Graduated Retirement Pension Scheme (SGRPS)) and a state flat rate pension. In the period leading up to its formulation the government, as is usual, set about a detailed consultation process on the funding of pension benefits, its thinking being highlighted in the White Paper – *Provision for Old Age: The Future Development of the National Insurance Scheme* (Ministry of Pensions and National Insurance, 1958). It had delineated its objectives as being threefold:

1. To place the NI scheme on a sound financial basis.
2. To institute provision for employed persons who cannot be covered by an appropriate occupational scheme in order to obtain some measure of pension related to their earnings.
3. To preserve and encourage the best development of occupational pension schemes.

These are interesting in that they give insight into the Conservative government's thinking that expenditure, a 'vice' of the welfare system, needed to be curbed and this could be allied to the increase in income, at least for the employed, that would arise under the proposed graduated pension. Importantly for our purpose though, the third objective was bolstered by the mechanism of contracting out ultimately introduced by the National Insurance Act 1959.

The state pension founded on the system of NI contributions confronted the Conservative government of the day with what it perceived as a demographic problem – a recurrent and universal theme in the thinking of state pensions social policy. The problem that was identified was the relative increase in the ratio of pensioners within the population (in 1911 it was shown that one person in fifteen was a man over 65, in 1958 it was one in seven). As a result the burden of those contributing to the state scheme through NI had increased with the relative drop in contributors (and would continue to increase with projected increases in the pensioner population). Though considered, like contemporary discussions of this issue, primarily as a funding issue (DWP, 1998), obliquely, it is an interesting point that identifies (though does not address), inter-generational equity. The 'Pay As You Go' basis of British State Pensions places current funding risks on today's (and tomorrow's) contributors. Given the acknowledged reduction in the ratio of contributors to pensioners (also known as the 'support ratio'), this suggests, at one level, an increase in the (financial) risk borne by non-pensioner generations. Much of the discourse relating to this point – particularly governmental – considers, in somewhat pejorative terms the inter-generational 'burden'

borne by existing contributors (DWP, 2006b). Of course one response is to accept that as a matter of social responsibility and indeed in the promotion of social solidarity contributors, benefitting as they are of increases in productivity and efficiency, are best placed to shoulder this responsibility, and we have in mind and prefer the collectivist view of social solidarity both in terms of mutual support and risk sharing (De Deken, et al., 2006). Moreover, there is some evidence, albeit a complex response to a complex issue, that contributors accept the necessity of this responsibility and the increase in their financial stake in the pensions payable to the old (DWP, 2006c). This is an important point when considering social cohesion and the responsibilities undertaken to promote fair treatment of pensioner citizens. It is an issue which also addresses the exclusion particularly felt by pensioner groups who disproportionately figure in the lowest income groups.

At that time also, rises in pension benefits for those in receipt were effectively being paid by current contributors, thus leading to benefits in excess of contributions. This required additional contributions from the state to fund the scheme to meet its obligations. Yet the NI scheme with its flat rate contributions and payments had accommodated, albeit at a minimum level, some pensioner recipients, particularly married women, where social conditions had resulted in large numbers not engaging in paid work or sporadic, low paid work. The receipt of pensions, for example, in the form of wives' or widows' pensions was acknowledged to rest upon communitarian values. This however was a government not on all fours with such values. A telling insight to this is identifiable in the White Paper (at page 5):

How best to make proper provision for the old is one of the biggest social problems of our time. Its importance and its difficulty are alike increased in a community such as ours in which the proportion of older people has risen and is going to rise further. It is vital, too, in considering public policy on this subject, to ensure that state action does not undermine the personal responsibility of each of us to make such provision as we can for our own old age. (Emphasis added).

This would not be out of place in a current government pension document. Similarly, the fondness for private pension provision is discernible elsewhere in the White Paper by the description of occupational schemes as a "National Asset" (page 5). Amongst the proposals to overhaul the NI scheme and to move away from a flat rate pension to a system of graduated contributions and pensions, is an ideological commitment to bolster self-responsibility for provision for old age - part of successive Conservative governments' thinking to a greater or lesser extent. This is the hallmark, in some respects, of latter day social policy whereby those that can provide for their future, be encouraged both financially and structurally, to do so. This was a government then, concerned to reduce the economic cost of the state scheme whilst at the same time promoting, fostering and providing an incentive to the development of private schemes. The Minister for Pensions and National Insurance, John Boyd Carpenter, saw the introduction of contracting out as vital to encouraging the private sector. These provisions should be seen against the wider pensions debate at that time with the Labour opposition plans to 'market' a more generous, but nevertheless re-distributional (and it might be said complicated), scheme which supplemented the pension incomes of the poor, with the middle and higher earners only marginally better off (Hannah, 1986). The Labour party would be given a chance to implement this policy between 1964 and 1970, but would fail to do so. And as Hannah (1986) notes it was the private pension interests (for example, employers' organisations), which was the effective opposition to such plans.

### 1975-1979: The Castle Reforms

Aside from the abortive attempt by the Conservative government to abolish the graduated element of the state pension and replace it with what was termed a reserve pension – with benefits linked to investment performance - in the Social Security Act 1973, the National Insurance Act 1959 provided the mainstay of British pensions policy over this period until the Social Security Act 1975. A Labour government was elected in 1974 with pensions social policy being a key piece of its approach to welfare. The party's earnings related proposals, which had been simmering since the 1950's, were brought to the boil, with the result that pensions targeted the needy and those who experienced sexual inequality. The recognition that social exclusion based on ethnicity had, up to this point, little discourse. The great irony of the Beveridge welfare reforms in the 1940's, is that they were predicated upon a narrow view of the role of women in employment and more particularly in the home. In the 1975 Social Security Pensions Act, a flat rate basic pension and a state earnings related pension (SERPS) were established, and were linked to a person's earnings factors, originally the best 20 years, but later a career average. The earnings factors were linked to a band of earnings between what was known as the upper earnings limit (UEL) and the lower earnings limit (LEL). These were re-valued every tax year to reflect any increase in average earnings up to retirement age. The self-employed were not eligible, nor were those earning below the LEL or those with no earnings at all. The maximum value of SERPS was 25% of the relevant earnings, subject to the person having at least 20 years working life remaining between 6 April 1978 and the state pension age (SPA). Benefits for those with less time remaining before SPA had a pension which was proportionally reduced. The Act provided that the basic rate pension was uprated in line with prices or earnings, whichever was the greater, whereas SERPS was uprated in line with prices only. An occupational scheme could contract out of SERPS provided it offered a guaranteed minimum pension (GMP) which was equivalent to SERPS.

The difficulty in part for the Labour party was the ability to draw some sort of political consensus for its plans, both state and private, for an area of social policy and law that required a longer term commitment, rather than the short cycles of policy, so concomitant of the electoral successes of the two main political parties and which had dogged pensions policy. What is particularly interesting about Labour's pension policy and its continuation of contracting out, is that certain interests within the party, particularly the trade unions, were no friends of the private (largely occupational) pension provision. This was seen as sporadic (as a result failing to meet the retirement needs of the majority of the workforce), promoting inequality and lacking in security (due to investment vagaries and legal and regulatory failings). Fawcett (1999) notes how prominent the trade union movement was in promoting pensions as part of Labour's social policy with the result that when in government, it became central to its policy on welfare. However, its commitment was to a real increase in the flat rate element as opposed to the earnings related element, which the party had courted for some time. In fact during the years 1974-1975, when inflation was high, this link was essential to enable pensions to be kept in line with the national standard of living. The position in relation to contracting out at this time would appear to demonstrate a government's acknowledgement of the benefits that private pensions, particularly occupational, provided for those members of such schemes on above average incomes. Its focus with regard to its pension proposals was the majority of pensioners, current and potential, who faced the future with lower incomes. Indeed the private (occupational) sector, facilitated as it was by contracting out, could do nothing for those excluded from the workforce. The new earnings related element significantly increased the level of income for the majority of the workforce and indirectly uprated the benefits for those in lower paid work

in contracted out schemes by the equivalence requirements of the benefits available under SERPS, that is, in terms of a guaranteed minimum pension. The fascinating and often overlooked point is that the collective or communitarian principles driving the state scheme became an indirect stimulus to the private sector provision to raise the pensions for the lower paid. This is an obtuse and not directly discernible symbiotic relationship between private (market) pension arrangements and the state pension addressing the needs of the lower income (working) groups. It is generally assumed that the private market-based sector of itself cannot sufficiently address the needs of lower income groups for a variety of reasons – sporadic provision, cost, etc. Governmental responses at that time, predicated as they were on both market structuring/promotion, were not entirely incompatible with broader social justice led thinking with regard to lower income groups. Of course, this does nothing for those in the lowest income groups by way of being excluded from the workplace by age, gender, ethnicity or disability. This latter point was (and is) seen to require a general welfare response, focusing on short term thinking so bedevilling pension policy. Exclusion from the workplace and the well-documented benefits associated with work activity for those who can raises the undoubted corollary that exclusion becomes, particularly for those below pensionable age, a continuum into pensionable age.

### **1979 -1997: The Cult of Popular Capitalism**

1979 saw the election of a Conservative government with a radical reformist approach to the welfare state. Pension policy changed direction for the next 18 years. The government's concern for reform seemed to centre on its perception of the welfare state – and particularly the state pension - as being excessive in terms of cost, notwithstanding that, as Creedy and Disney (1989) suggest, the *raison d'être* for this as the guiding principle is ill-elucidated in the government literature. Its putative tendency was to create little or no incentive for state dependency. As is well documented, it was also a government committed to the reform of public service and public service provision by the wind of change that market forces and market ideology would blow through the public sector: the collectivist ethos of a state pension was to be deprecated and was antagonistic to this political philosophy. This approach and successive legislative measures would result in significant effects for the poorest members of society in the reduction of available benefits and in valuations of benefits. Early in its second term of government it set about a period of planning and consultation for major reform of the welfare system. A policy objective buried within its proposed reform of the state pension structure and one which should be viewed against the ideological backdrop of this government, was the desire to encourage the saving for retirement through private means – the market being the most efficient and effective vehicle for ensuring appropriate saving. SERPS posed a threat to this idea, since it represented a disincentive to the accumulation of an occupational pension. To this end, the government proposed the abolition of SERPS in favour of an enhancement in the basic pension and a major shift to private and occupational pensions and other forms of saving investment, such as home ownership (Department of Health & Social Security 1985). Ironically, the thinking of this government relating to compulsory employee membership of occupational schemes, albeit without the element of compulsion, re-surfaced under New Labour (DWP, 2006b). Pensions were viewed by the government as another aspect to the cult of popular capitalism which it peddled. Whilst ultimately SERPS remained, albeit in modified form, to promote its policy of increasing private saving, the government reduced the value, and particularly the attractiveness of SERPS by basing the accrual on the lifetime average earnings (as opposed to the best 20 years), and reduced the maximum pension payable to just 20% of earnings (as opposed to

25%). Against this, and concomitant with its predilection for individual sufficiency and ownership of and involvement in wealth creation, it proposed the move from SERPS to personal pensions and to a lesser extent occupational pensions; a move not without its difficulties. Personal pensions providing money purchase benefits came to the fore during this Conservative government and was introduced in the 1986 Social Security Act. This was a government that introduced the 2% incentive for people leaving their company schemes and taking out personal pension schemes. This undoubtedly related to an agenda that sought - from both social and fiscal policy objectives - to maximise directly and indirectly individual autonomy, responsibility, choice and, as an assuage to the market, mobility and flexibility. This latter point was thought to counter the drawback with salary related schemes which militated against portability within the jobs market. The government spoke of its desire to increase 'popular capitalism', and personal pensions with their putative relevance to a modern jobs market, was, like share and home ownership, an important part of this. The deprecation of the occupational pension scheme, with its attractive guaranteed final salary scheme, was also seen by the right wing of the Conservative party as a devious and underhand form of socialism: they did not involve the employees in that feeling of participation of wealth creation. Needless to say, those not engaged in paid work were addressed by a stricter regime of welfare benefits.

### **1997- 2010: New Labour**

'New' Labour came to power in 1997. Over nearly 13 years it produced an astonishing amount of governmental activity in terms of pensions policy discussion, research, consultation (through its main conduit the Department of Work and Pensions and the short-lived Pensions Commission) and legislation. Very quickly it put its welfare reform agenda to the public - pensions being at its core. In December 1998, it published its first major discussion document. Some of the policies promulgated in this document would not look out of place in an old style labour government, but the thinking had been informed by the later social democratic ideology that accepted the role of the market, albeit engaged with state control, to address and facilitate social policy options in pensions that address social justice issues of need, worth and opportunity (DWP, 1998). We are able to identify four main threads to pension policy at the end of the 1990s.

1. A strong re-distributional element, with 'state aid' going to the lowest paid;
2. The public-private partnership, so beloved in other areas of labour party policy played an important part in pension reform;
3. Linked to 2 and underpinning much labour party policy on pensions, was the need to keep a check on public expenditure; and
4. Contracting out was still, at this stage, seen as an important aspect of achieving the government's objectives in pension reform (linked as it is to the privatisation of pension provision).

A new second tier State Second Pension (S2P) was established in the Child Support, Pensions and Social Security Act 2000 (the basic state pension remaining in place for all with appropriate NI contributions), to replace SERPS. Greater emphasis was laid on a reallocation of pension resources to the lower paid and those unable to make appropriate compulsory NI contributions (for example, carers). In order to achieve this S2P would ultimately be worth double the rate of SERPS for those earning below £9000 per annum with the benefits for those earning between £9000 and £21,600 (re-valued from the original £18,500), being

increased but tailing off. These rises in S2P would not be available for higher earners. Moderate and higher earners would de facto have recourse to the private sector. This of course was predicated upon the Stakeholder Pension and appeared to assume the success of the same. However, what was still discernible, even under this admirable attempt to assist the lowest income groups, was the drive to ensure that the majority of income retirement was ultimately borne by the private sector. The stated objective was that the majority (60%) is so provided. To do this the government increased NI rebates to provide incentives to join private schemes (particularly for moderate earners), made S2P less attractive (particularly for moderate earners), and introduced its 'flagship' low cost, flexible private scheme, the stakeholder pension. In line with all previous initiatives, stakeholder schemes were to be ultimately a replacement for SERPS/S2P for moderate earners as they were permitted by the legislation (with added incentive) to contract out of the second tier state pension. This placed explicit faith in the private sector to be able to provide the majority of pension provision in the future; the stakeholder schemes apparently provided the mechanism for lower and moderate earners to enter the private sphere without the associated financial problems that can arise with some personal pensions. In terms of the position of the lowest income groups – almost invariably not engaged in the workplace – continued emphasis was placed upon (means-tested) welfare benefits.

A communitarian spirit prevailed (as did the private-public partnership), in the entitlement for all contributors to receive a (basic) state pension. The reality behind financial incentives and legislative initiatives to promote private provision – and contracting out is (or perhaps, was) a significant feature of this development – is that this has focused the state scheme on the lowest income earners. Whilst the broader social justice position undoubtedly required some re-focus upon the income position of the lowest income groups, the effect of this was, to a large extent, to marginalise the relevance of state pensions for large numbers of workers in its ability to provide a pension that reflected, or at least attempted to provide, income that was commensurate with working life earning capacity. It would seem that this has become an accepted part of the promotion of market-based provision. Modern pension trends have thus been promoting a pension expectancy for old age based on private, investment related performance. Individual (that is through the market) as opposed to collective responsibility for retirement income is commensurate with the social democratic approach to public welfare prevalent in both the US under Clinton and the UK since 1997. The UK placed and is placing a huge amount of 'hope' in ability of the market to be able to provide appropriate pensions in the face of demographic changes and increased life expectancy (and it must be added, stable and positive economic conditions which recent times show to be misplaced). It could thus be asked whether the state scheme and associated benefits are once again mainly concerned with the amelioration of relative poverty?

In its Green Paper (forming the basis of the Pensions Act 2004 and the Finance Act 2004), the government continued with proposals for pension reform (DWP, 2004a). Unusually, the re-distributional element, which was so prevalent in its previous Green Paper, was less obvious here, with the paper addressing the reasons why people fail to make adequate provision for retirement. This had been a consistent theme that the government had sought to address in its contemporary pensions policies. Clearly, part of the guiding philosophy was that individuals can and should, where possible, be instrumental in providing adequate pension income through opportunity (by appropriate products and informed choice) to address their later life needs.

One of the government's central beliefs as to why people have inadequate pension provision was due to the complexity of the pension system and the complexity of the products available to the individual. In order to address this, the government suggested a simplified pensions tax framework be introduced (the Finance Act 2004), and that contracting

out too was in urgent need of simplification (it should be noted that 'simplification' in the context of pension legislation, is a relative term). There is no doubt that an indirect (and deliberate) result of simplification was the reduction of the costs to employers. The government in its Green Paper and the Pickering Report both believed that contracting out should remain, but with some amendments (DWP, 2004a; DWP, 2002). Several alterations to the contracting out mechanism were floated, including the removal of the requirement to provide survivors' benefits (a recommendation of the Pickering Report, which the government said would have a disproportionately negative effect on women); the simplification of the Reference Scheme Test (RST -which was the benchmark which a final salary scheme must satisfy in order to contract out of S2P); that the requirement that must be met in order that a scheme meet GMP be made easier; the lump sum restriction be removed, which has meant that contracted out rights could not be commuted as part of the lump sum, and the revision of the age restriction relating to contracted out rights which would mean that schemes started to pay out all the elements of a pension at the same time.

There is little doubt that the crystallisation of some of these ideas (for example, making it easier for schemes to achieve RST) into legislation would have resulted in a reduction of members' benefits, but in order to achieve simplification of the system the government showed its willingness to sacrifice the level of a certain section of society's pension benefits. Some respondents to the Green Paper opposed contracting out though they had only to wait a short time for their view to be followed.

Very few of the ideas relating to contracting out in the Green Paper found their way into the Pensions Act 2004, and the Act did little more than tidy up existing legislation. The provisions relating to the minimum age from which protected rights could be paid were removed, enabling them to be paid at the same time as all other rights. This should result in a simplification in the administration of contracted out regimes.

A remarkable volte face on contracting out occurred by the time of the White Paper, *Security in Retirement: Towards a New Pensions System*, based as it was on the work of the Pensions Commission, (DWP, 2006b). No longer did it have a place in the future of pension provision in this country, but rather its complexity and inherently elitist nature (favouring and benefiting those workers with higher earnings) heralded its demise. The re-distributional element that had been such a central feature of the 1998 Green Paper again resurfaced as the core of pension reform, with personal responsibility for pensions, fairness to all and the recurrent theme of simplification of the system being the primary foci. The recommendations of the Second Report of the Pensions Commission (2005) on contracting out were warmly embraced. It has to be noted that neither the Pensions Commission, nor the DWP explicitly recognise the potential inhibitor that contracting out is to re-distribution and we suspect that the rise in the numbers contracting back into the state scheme with the correlative affect upon future increased S2P liabilities were relevant to the decision though both publications suggest the causal mechanism for this to be 'complexity'.

Given the relative lack of success of the earlier Stakeholder Pension, the introduction of low cost personal accounts would give those who did not have access to an occupational pension scheme an opportunity to save (DWP, 2006b; DWP, 2006d). People would automatically be enrolled into either their employer's scheme or a new personal account with the ability to opt out. This is now contained in the Pensions Act 2008 which, inter alia, will bring an end to the Stakeholder Pension and provide for the ultimate establishment of the National Employment Savings Trust (NEST). There are of course, some concerns with automatic enrolment in personal pensions. For some workers it may not be the best method of saving and even for those whose pension saving is addressed by automatic enrolment (and it must be conceded that in principle, requiring saving has merit), funds will inevitably be managed, incurring charges, and will depend upon future annuity rates that may turn out to

provide poor value. The state system will be 'simplified' with S2P becoming entirely flat rate by 2030 (though this is currently being considered as part of the current Coalition government's consultation, with one option being the acceleration of 'flat rating' to 2020 (DWP 2011)). Thus, from 2010 it was suggested that the state pension be made fairer and more widely available. An inherent aspect of this simplification and fairness, said the government, would be the abolition of contracting out for defined contribution occupational pension schemes, and appropriate personal pension schemes. The complexity of the area, however, is such that reform has to be staggered (particularly in relation to defined benefit schemes). Contracting out was accordingly abolished by the Pensions Act 2007 for both defined contribution and appropriate personal pension schemes in order, it was said, to provide greater clarity, and to reduce administrative costs. The anticipated abolition date for this is 6th April 2012. In relation to defined benefit schemes, contracting out is to be phased out by 2030. While the abolition of contracting out does undoubtedly simplify the pension system in this country, its abolition also has a re-distributional basis. In 2002-2003 contracted out rebates amounted to £11 billion (for the 'doomed' DC schemes, around £2.6 billion annually) one third of pension contributions. Once the abolition of contracting out is complete it means that these rebates will be available to provide state pension provision to the lowest earners, carers and woman who were promised better provision, and who would not have sufficient contributions on their own merits. Furthermore, the effect of the abolition of contracting out for final salary schemes (which were probably seen by the government as regressively distributional), will mean that the contracted out rebates will not be available for investment purposes, worsening the plight of these schemes still further.

### **2010 to Present: The Coalition**

On the 6th May 2010 Labour lost the general election, bringing to an end, some 13 years of unbroken governance. The 'victors', if it be accurate to describe them as such, were the Conservatives who were though unable, without a coalition agreement with the Liberal Democrats, to form a government. The resultant coalition government has forged an unlikely alliance between two political parties who share, on the face of it, only marginal ideological similarities though on some issues, as it were, 'they speak the same language but with different dialects'. In relative terms, the shortness of the period of which the coalition has governed has meant that pension changes, insofar as they can be dealt with, have largely concerned maintaining changes brought about by legislation in the last parliament: particularly that relating to age equalisation for men and women and the increase in the retirement age although it has proposed a correlative acceleration of the increase in the retirement age. However, one should not under-assess the current, and no doubt future, efforts of this government to foster market-based pension provision. Also, and importantly for pensions provision, the tenets of the Equality Act 2010 (a measure of the last government) means that provisions in relation to gender, race, sexual orientation must be considered in relation to the provision, alteration, consolidation etc of pension provision. Some good news for pensioners in receipt of state pensions was the restoration of the link with earnings as a basis for up-rating the basic state pension. Current government consultation appears though to be centrally concerned with the cost of the state pension system and a consideration of measures designed to increase workplace and personal saving. The establishment of the NEST scheme, endorsed by this government, places huge hope on the market mandated provision of workplace (not necessarily occupational) pensions with the scheme, though administered by the legal panacea, 'trustees', ultimately in the hands of investment managers. Whether this will provide a good deal for pensioners in such schemes is of course, moot.

### *Contracting out*

Considering this point in broad terms, contracting out of the higher or second element of the state pension is, in essence, a simple idea but the allurements that simple ideas have is diminished in this context with the veritable ‘Gordian Knot’ of legislation and policy changes over the period. The state provides a basic contributory pension – through NI contributions by both the employed (including the self-employed) and employer - whilst at the same time providing higher benefits, with a financial ceiling, over and above the basic pension by virtue of increased NI contributions. It is this latter element that a person may ‘contract out’ of, though the decision is, on the whole, not one of individual choice. In truth, the system is thus one of partial contracting out. This means that the market place through appropriate occupational or personal pensions, provides the higher benefits (with a ceiling limited only by the earning and/or saving capacity of the pensioner), where there has been contracting out. Thus there are two types of private pension relationships with the state scheme; those which are contracted out of the (second element) state scheme, and those which are not contracted out (sometimes referred to, if inaccurately, as ‘contracted-in’). Whilst not all pensioners are required to have contributed to the basic state pension (for example, married women), it is the payments received by the state through NI contributions from those with earnings between specified lower and upper levels of earnings that also fund the basic element and those that contract out continue to contribute by virtue of reduced NI contributions. In essence a redistribution of resources takes place from those making NI payments to fund low-level pensions for all (including those who have not made or made insufficient NI contributions). As noted, this is a continuation of the original welfare communitarian ideals prevalent in the UK throughout the major part of the 1940’s. Whilst this redistribution may be seen to be a worthy social and indeed policy goal, the extent of redistribution within the British pension arrangement is not entirely obvious, nor is it achievable within desired limits. A system which permits earnings related benefits (as opposed to purely flat rate benefits with earnings related contributions) and partial contracting out makes a redistribution of resources even more marginal (Creedy, 1982) which has profound effects for the lowest income groups, and the move of S2P to flat rate benefits with earnings related contributions facilitates a redistribution. Thus the extent to which a broader social policy objective of horizontal redistribution, targeted as it is on those in the lowest income groups, is achievable is moot.

Why should the state legislate for a pensions competitor? Whilst a number of motives, both intended and unintended are discernible, it is by no means obvious why this has taken place. The state could, for example, have provided both basic and higher elements as a sole provider or have funded more generous higher benefits and required any market place competitors to match these, or at least made it extremely difficult for it to do so. Indeed this has on occasion been part of mainstream (left wing) thinking. However, private and in particular occupational pension provision has for both the privately and publicly employed been a major part of the UK fiscal and political approaches to retirement age saving.

To put the provisions into some sort of context, some 16,200 public and private occupational pension schemes in the UK are contracted out, the majority being made up of private sector schemes. There are around 9.2 million active members of contracted out occupational public and private schemes (Government Actuary’s Department (GAD), 2003: Later figures for the same period (2003/4) suggest 11.1 million (DWP 2007)). Figures for this period also suggest that there are approximately 5.5 million APPs (including Stakeholders) with the trend suggesting a decline in numbers. While the concept of contracting out may be relatively straight forward, the relevant legislation and accompanying regulations are extremely

complex. Within the confines of this paper, it is proposed to provide a broad outline of the mechanisms.

Contracted out OPS are required to use the state scheme as a benchmark for pension provision. This was enshrined in the original legislation as the requirement that a contracted out scheme provide (at least) a guaranteed minimum pension (at least equal to SERPS/S2P). This was replaced as from the 6th April 1997 by what is termed the 'statutory standard'. The statutory standard itself is preferable to a statutory description of what is termed a 'reference scheme test' – a basic acceptable outline of a pension scheme providing benefits equivalent to the state benefits given up. So, for employed earners, this means inter alia, that they are entitled to a pension at the normal retirement age commencing at 65 and continuing for life, and for the annual rate of the pension accrual to be 1/80th of the qualifying earnings in the final 3 years of service, multiplied by the number of years' service.

These criteria are unsurprisingly not difficult to match. On the whole, for employees who are members of an OPS (including a stakeholder scheme), the decision as to whether to contract out of SERPS/S2P does not lie with them, but their employer. Employers can discriminate between employees in terms of the decision to contract out or not in relation to the nature of employment, but are otherwise prevented from discriminating (for example, in relation to gender).

An employer proposing contracted out employment must give notice of its intention to contract out and engage in a period of consultation with its employees and any independent trade unions concerned with those employees, relating to its intention to contract out. In addition, consultation will include any trustees of the scheme, scheme administrator and any insurance company or Friendly Society. This must be done within a statutory minimum 3 month's notice period. These statutory requirements are no doubt supplemented by a common law requirement that the employer conduct itself in a manner not calculated or likely to destroy or seriously damage the relationship of confidence and trust between employer and employee without reasonable and proper cause (the 'obligation of good faith'). Largely, the mechanics of contracting out, maintenance of this status and cessation, are dealt with by H. M. Revenue and Customs. This is also true of personal pension schemes (referred to as appropriate personal pension schemes), and like much pensions legislation and associated regulation, can exhibit tensions between fiscal policy and social policy. During the period for consultation, any disputes can be referred to an Industrial Tribunal. Though the substantive nature of the consultation exercise is not stipulated, the general law would seem to require a meaningful exercise.

As has been noted, the issue of a contracting out certificate in relation to a contracted out salary related scheme (COSRS – or defined benefit scheme) and contracted out money purchase scheme (COMPS – or defined contribution scheme) means that both the employee and employer pay reduced NIC's (known as the contracting out rebate). For COSRS, the combined rebate for NICs from April 2007 is 5.3%. The rebate has been steadily reducing over the years and has led to the potential re-contracting back into the state scheme – thus the rebate needs to maintain a level of attractiveness. To counter this, the rebate has increased from a total rebate of 4.6% from the previous period (though not to the extent as advised by the Government Actuary). This demonstrates the extent to which policy prioritises, and the fine line between, fiscal and social policy.

COMPS are an alternative to COSRS, being based on a money purchase (defined contribution) basis. These schemes were introduced in the Social Security Act 1986. A variation permissible since 1997 is, as it were, the running of two pension streams in the same channel. This is where a contracted out scheme has one part contracted out as a COSRS and another as a COMPS – known as a contracted out mixed benefit scheme (or COMBS). This permits the contracted out basis of the scheme (commonly the COSRS) to change to a

COMPS to seek the higher rebates available there under. The contracted out rebate rate of NICs is applicable. Until 1997, this was the same as that for the COSRS. Different rebates were introduced in an attempt to provide via financial incentive (or rather disincentive), a policy lead in the basis of contracting out. That is, the rebate for COMPS was reduced to make it clear to schemes that it was preferable to contract out on a salary related (or defined benefit) basis. Again the social policy objective relating to the putative long term benefits of salary related schemes and the advantages for retirement income replacement was led by fiscal means. For example, the total rebate from 2002 is 2.6%, having been slightly increased from the 1999 total rebate of 2.2% (compare COSRS rates above). Additionally, in the same period, age related rebates for COMPS sought to provide a disincentive to re-contract in. Indeed, the Pensions Act 2007 abolishes contracting out for COMPS and APPs with effect from 2012 or soon afterwards.

Notwithstanding these incentives and disincentives, it has been apparent that the attractiveness of COMPS has been diminished. This is in large measure due to the assumed investment return rates which have, at least of late, proved rather optimistic.

Ironically over the same period, there has been a trend for larger OPS salary related schemes to either switch to a money purchase basis, or close their salary related schemes to new members and provide money purchase benefits instead, and the government policy of taxation of dividends since the Finance Act 1997 has contributed to this.

APPs have featured since they were established in 1986 and an APP is one which is authorised for contracting out and will also have an appropriate contracting out certificate issued. In conforming with the requirements for personal pension schemes (based on one of two model rules contained in the Income and Corporation Taxes Act 1988), they (and COMPS), had to have a protected rights element, though this is to be abolished. The abolition of the protected rights element – particularly the survivor's benefit – appears to suggest that the government was prepared to run the risk of worsening the position of (largely) women reliant upon their husband's pension. The government appeared to rely upon a position where it asserted that most annuities are single life – this in a publication directed inter alia, at “fairer outcomes and gender equality” (HM Government, 2005). This overlooks (or at least simplifies) the position of COMPS which are required, at least to date, and until the combined effect of the Pensions Act 2007 and the Pensions Act 2008 come into effect, to have a protected rights element.

It has been noted that the policy motives behind the 1986 Act's provisions related to the spread of ‘popular capitalism’ and the direct benefits in terms of savings to the state scheme that would result as a consequence of the numbers of APPs. Interestingly, the government provided an additional financial incentive in this respect of 2% of relevant earnings for the years 1987 – 88 and 1992 – 93. For the years 1993 – 96, this was reduced to 1%. Also, the legislation included prohibitions on employers obliging employees to join company schemes and facilitated the move by employees who wished to leave company schemes in favour of personal pensions. The wisdom and/or the desirability of the removal of the compulsory joining of a company scheme was part of the general debate by the previous government concerning the increase in retirement saving; it was convinced that an element of quasi-compulsion is preferable in achieving increased saving.

Members of APPs (including those where an employer contributes) pay NICs at the full non-contracted out rate. That is, they rely on the rebate (with appropriate tax relief thereon), being paid direct to the scheme by the H.M. Revenue and Customs. Levels of contributions, both minimum and maximum, are controlled by legislation and are as a result, a significant driver in the achievement of the policy aims.

One further point that should be noted in relation to contracted out schemes, whether they are defined benefit or defined contribution (including APPs and stakeholder pensions), is

that in relation to rights accrued since April 1997, the state has divested itself of any responsibility to increase pensions (or at least the contracted out element), in line with inflation. The Pensions Act 1995 required that Limited Price Indexation, of the lower of the Retail Price Index (RPI) or 5%, was borne by schemes themselves. This has added considerably to scheme costs. The Pensions Act 2004 reduces this requirement, perhaps more realistically in the light of the levels of inflation in the UK, to the lower of the RPI or 2.5%. As we have noted above, with regard to DC schemes, contracting out is to be abolished.

### *Policy Trends*

The UK experience with contracting out over the last 51 years could lead one to conclude that in many respects it has been something of the proverbial curate's egg. Undoubtedly, this has in large measure been a result of the lack of clear policy objectives by successive governments at this, for the UK at least, a vital interstitial meeting point of the private and public sector. Moreover, the lack of substantive political consensus and the relative 'short-termism' in both policy and legislative creation, has not allowed governments to engage in thinking about pensions policy much beyond a 20 year time scale. Insofar as it is possible to discern them, a number of desired policy objectives are evident and it is possible to include a number of separate objectives under broader headings where they exhibit a degree of homogeneity. The ability to achieve or carry these through is, given the above, difficult to assess and conversely at times oblique, unintended and undesirable consequences have followed.

*Income replacement.* Workers on the whole have an expectation of income in retirement that reflects their working life income. Of course to maximise the income received in retirement requires suitable, notwithstanding the holding of other assets, saving during periods of work. In this way, workers could expect that their saving patterns would provide an acceptable income replacement ratio in retirement. The government assumed this ratio to be somewhere between a half and two-thirds of final gross earnings (DWP, 2004a). It is suggested that contracting out has been a significant initiative (though not the only), in driving the expectations of workers, through private pension provision, of appropriate income replacement levels. The reality is somewhat different. The majority of workers have no private pension provision and these workers are concentrated in the lower income groups and show a high proportion of women, with a resultant disproportionate gender impact. The latter point is important in the context of the duty placed on the government to assess such impact (i.e. the effect upon, inter alia, gender equality) as a result of the Equality Act 2010. This has significant consequences for any policies aimed at raising the level of pension related saving and directed to create inclusive opportunities for the lowest income groups. The relatively high amount of saving within the UK is skewed because of the disproportionate amounts saved by the higher income groups. Whilst the government's recent measures in relation to S2P will, it claims, for the lowest income group provide at least the higher of the desired replacement rate (possibly 100%), moderate earners (those earning between £10,000 and £20,000) will struggle to achieve the income replacement rates commensurate with earnings and certainly the weight placed upon stakeholder pensions in this respect is too great to bear. Personal Accounts (and NEST) are expected to be able to address this. In part this is because there are some 8 – 13 million people, again concentrated in the lower income groups, whom the government believed are "seriously under-saving for their retirement" or who "may want to consider saving more [and/or] working longer" (DWP, 2006b). As such, for the lower income groups, contracting out would seem to be of little relevance. The income gap as such is exacerbated into retirement.

*Relief of poverty.* Pensioners overall in the UK have over the last 50 years seen incomes rise faster than the working population (Hannah, 1986, p.54). In the period 1979 – 1996/7, average net income in real terms for all pensioners rose by some 64%, compared to a 36% rise in real terms for average earnings. In the period 1994/5 to 2002/3, average net incomes for pensioners have risen in real terms by 25% compared with a rise in real terms of 13% for average net earnings over the same period (DWP, 2004b). These rises in income have not been shared by the poorest pensioners to the same extent, the major sources of income growth being attributed to occupational pensions (which increased by 162% in real terms between 1979 and 1996/7), personal pensions and earnings. Around 51% of average gross income for pensioners still comes from state benefits (DWP, 2004b). The divide between the poorest pensioners (relying on state benefits) and the wealthier pensioners whose income has grown as a result of occupational and private income, has increased. Contracting out has, at least for those eligible, been intended to attempt to achieve or at least facilitate, a retirement income commensurate with working life earning capacity beyond that which the state is willing to provide with its approach to compulsory saving or contributions: the lower proportions of direct taxation comparable with other EU countries (that is income tax and national insurance contributions), illustrate this point. As such, for the (eligible) working population the private sector has been the desired – particularly by governments – means of avoiding relative poverty. It is now undoubtedly the mainstay of current pensions policy. Contracting out has been a significant contributor to the encouragement of private pension provision. The evidence is that the private sector has thus been very successful, relative to the pensioner and working population at achieving the rises in income. This has, as an indirect result, increased the schism between the poor and wealthy pensioners – of course breaking the link between pensions and earnings has contributed to this. In an era largely dominated, at least latterly, by the adoption of broader social justice values, which recognise the importance of adequate income to facilitate inclusivity, this must be rather difficult to accept. Indeed little comfort will be gained in this respect with the recent evidence of increasing pensioner poverty.

*Market Enhancement.* The original motives for contracting out were undeniably to promote the private market in pensions. Subsequent governmental moves have built upon this original idea, the creation of the APPs is apposite here and of course the hope of the previous and current government is that ultimately the market place would provide some 60% of retirement income. As a corollary two further points arise, viz, by necessary implication, the facilitation of private retirement income would occur and the changes in work patterns over the last 40 years, particularly the greater use of short term contracts and particularly for women, career breaks, required a more flexible approach to work based retirement saving (for example, portability of pensions). Certainly, changes in pension provision have facilitated this. These points though mask what is an obvious if subtle exercise in ideological symbiosis in that contracting out by both occupational and personal pension, particularly the latter, encourages workers and pensioners to effectively ‘buy into’ the tenets of the market based ideology.

It is difficult to conclude upon the achievement or otherwise of this genre of policy objectives, but one can highlight the relative success of the private pensions industry in the extent of provision and the levels of retirement income relative to other sources of income over the period. Significantly for the UK as well, private pension saving has contributed to overall national prosperity both in terms of pensioner income and in relation to the market contribution made in terms of asset strength and investment (DWP, 1998; GAD, 2003; DWP, 2004a). This success has come at a cost. In some quarters, the excessive reliance upon the private sector has been called into question as a result of stock market falls between 1998 and 2003 (House of Commons Work & Pensions Committee, 2003) and of course, 2008. The

sheer complexity of contracting out and the resultant burdens, administrative and financial, upon schemes provide obvious drawbacks. If we accept the part that contracting out has played in this success, then it must also be said to have played a part in building up an expectation of success and security in private pension provision. That said, however, there have been notable episodes where the trust in these modes of provision has been severely undermined and, we would propose, suggest a similar undermining or loosening of natural community bonds – a marker of collective well-being and integration for the retired in particular - whereby the belief has been engendered that the State will not now provide adequate resources in old age despite significant contributions over the working life and that “personal saving” (in whatever form) is to be promoted.

The State: its social and societal benefits. A number of mixed factors arise here and it is not concerned exclusively with economic savings, but included is the redistribution of resources. This is an intended if perhaps indirect policy objective. Insofar as the pension structure within the UK is required to achieve this, it is extremely moot, given the combination of contributory first level (flat rate) and second level (higher) benefits, whether this is achievable to any desired degree. The position of contracted out second level benefits complicates this and makes such an objective marginal. The introduction of S2P and the move to flat rate benefits will make a redistribution of resources more achievable. By this, governments will hope to be able to concentrate pension resources on those with traditionally lower incomes in retirement (particularly women). However, governments have acknowledged the continued reliance upon means-tested welfare benefits to help achieve this. The state has also intended to benefit itself by a reduction in the overall pension bill – the Pensions Commission itself noting that without contracting out, expenditure on pensions would be 0.6% of GDP higher in 2050 (Pensions Commission, 2005) - should the various proposals relating to contracting out and new scheme types (such as APPs and Stakeholder), bear fruit. It certainly benefits from the pre-funding of liabilities. In the face of the demographic changes over the last 40 years we have seen a decline in the pensioner support ratio. It is predicted that this could be particularly problematic in that the support ratio is anticipated to fall below 2 in around 20 – 30 year’s time, with resultant pressures on the NI fund. By encouraging and facilitating private pension saving, the state will not bear the level of costs (for example, as a proportion of GDP), that similar western economies are predicted to face. In this respect all looks well for the UK given the predicted decline in NI expenditure, suggesting a manageable and affordable expenditure (particularly as pensions spending takes up the majority of the expenditure of the NI Fund), as a proportion of GDP (GAD, 2000). Notwithstanding this drive toward reducing costs, governments have found a number of difficulties with the balance to be struck between the levels of rebate to provide a suitable incentive to contract out with manageable and sustainable costs. It has been noted how in relation to the introduction of the APPs, an additional incentive was provided in the form of a bonus in rebates. It has been estimated that in relation to the first period of bonus, the net cost to the NI fund (i.e. the gross cost of the bonus, minus the lower SERPS pensions), was £5.6 billion. The age-related contracted out rebates introduced in 1997 had, notes the Government Actuary (GAD, 2000, para. 7.20):

the effect of making contracting out less financially attractive at younger ages (lower rates applicable to the young). The fall in membership of APPs reflects the assumption that a much lower proportion of new employees after 1997 would choose to contract out through a personal pension.

Later figures put the contracted out rebate at around £8 billion. The National Association of Pension Funds provides further evidence that contracting out provides a poor deal and has led

to a reduction in the numbers of contracted out schemes (DWP, 2003; DWP, 2011). As we have noted above, there is evidence of members, particularly of contracted out DC schemes, contracting back in – undoubtedly hastening the demise of contracting out. From an employee's perspective, the rebate offset as a result of the ending of contracting out, will supposedly be neutralised by an enhanced or secured S2P provision in the future years. This does though raise the prospect of the state offsetting the risk attached to market investment with a secured future liability. Further, the effect of the introduction of S2P was to increase expenditure on the contracted out rebate by £1.3 billion in 2060/61 (GAD, 1999). The ability then, to manage and reduce public pension expenditure (particularly allied to the stated proportions of private/public pension provision of 60/40), is potentially stymied.

## Conclusion

The past 50 years has shown demonstrably the place that pensions have in socio-economic and political thinking. Contracting out has been, and is at least for the immediate future, an important piece of UK pensions social and economic policy. It has to an extent marked the place where ideological imperatives, generally ascribed to market led thinking, have wrestled with communitarian values. There are cogent arguments that pensions policy is today better served in the long term by the abandonment of contracting out, with resultant savings in terms of rebate costs redistributed serving an enhanced state provision and cost neutrality to employees – the government's own figures showing an increase in the numbers 'contracted-in' (DWP, 2003; DWP, 2011). However, governmental views in the UK have been beguiled by the market-oriented provision of retirement income. There is some evidence that for the most part though, the market has no relevance for the majority of the population and perhaps worryingly, has less attraction for many (DWP, 2003). Yet despite this, market enhancement has appeared to be one of the most significant generic drivers. It is debateable though whether contracting out did, or indeed can, serve any of the objectives normally identified with communitarian pension policies.

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