United Kingdom

United Kingdom: Pension system in 2020

The UK introduced a new State Pension system on 6 April 2016 for people reaching State Pension age from that date onwards. It is a flat rate scheme, with some transitional arrangements. For people who reached State Pension age before that date, the public scheme has two tiers, (a flat-rate basic pension and an earnings-related additional pension). Both are complemented by a large voluntary private pension sector. An income-related benefit (Pension Credit) targets extra spending on the poorest pensioners.

Key indicators: United Kingdom

		United Kingdom	OECD
Average worker earnings (AW)	GBP	41 807	30 559
	USD	53 599	39 178
Public pension spending	% of GDP	5.6	7.7
Life expectancy	at birth	81.1	80.6
	at age 65	19.8	19.7
Population over age 65	% of working- age population	32.0	30.4

Qualifying conditions

State Pension age is currently 66 years for men and women as of October 2020, rising to 67 years between 2026 and 2028. The Government has made provision for regular reviews of State Pension age, to take into account changes in life expectancy and other relevant factors. Under the pre 2016 system, an individual reaching State Pension age qualified for a full basic State Pension by: i) paying; or ii) having been treated as having paid; or iii) being credited with, National Insurance contributions, for 30 qualifying years in their working lives (between 2010 and 2016. Before 2010, it was 44 years for men and 39 years for women). A proportionally reduced basic state pension was paid to people with fewer than 30 qualifying years, to a minimum of one qualifying year of contribution or credits (for those reaching State Pension age between 2010 and 2016). People with no pre-existing National Insurance record prior to 6 April 2016 who reach State Pension age from 6 April 2016 will require 35 years of contributions to receive a full new State Pension amount, and the minimum qualifying period will be 10 years. For people with an existing record at 6 April 2016, transitional arrangements take an individual’s National Insurance record before 6 April 2016 into account, plus further qualifying years from then onwards, in most cases.

Benefit calculation

Basic and new State Pension

The standard minimum State Pension for a single person is GBP 177.10 in 2021/22, and GBP 270.30 for couples.

Workplace Private Pension Provision

Between October 2012 and February 2018, the government rolled out automatic enrolment into workplace pension schemes. All employers now have a legal duty to enrol all qualifying workers aged between 22 and State Pension age who earn over GBP 10 000 in 2020/2021 into a qualifying workplace scheme. In 2018/19 minimum contributions were 5% of a band of earnings between GBP 6 032 and GBP 46 350. In April 2019, minimum contributions increased to 8% of band earnings, and remains at this level in 2021.

To support automatic enrolment, the government established the National Employment Savings Trust (NEST), a trust-based occupational defined contribution scheme, to ensure that all employers are able to access a good quality, low cost pension scheme. NEST has a public service obligation to accept all employers that wish to set up a pension scheme with them regardless of their income.

Targeted

Pension Credit, is a tax-free weekly benefit for pensioners who are living on low incomes, which tops up their income to a certain level. Pension Credit is an income related benefit and is not based on National Insurance contributions. There are two elements to Pension Credit, the Guarantee Credit and the Savings Credit. The Guarantee Credit ensures a minimum level of income by providing financial help for people who have reached the qualifying age (see below) and whose income is below their "appropriate minimum guarantee". The appropriate minimum guarantee is equal to the Standard Minimum Guarantee (which in 2021/22 is GBP 177.10 per week for singles and GBP 270.30 per week for couples), plus additional amounts for people with severe disabilities, caring responsibilities or certain housing costs.

The savings credit is an extra amount for people over State Pension age who have made a modest provision for their retirement. Savings Credit is paid at GBP 0.6 for each GBP 1 of income above the Savings Credit Threshold (which in 2021/22 is GBP 153.70 per week for singles and GBP 244.12 per week for couples), up to the Savings Credit Maximum (which in 2021/22 was GBP 14.04 per week for singles and GBP 15.71 per week for couples). If an individual has income above their "appropriate minimum guarantee", i.e. they are not entitled to the guarantee credit, then each GBP 1 above their "appropriate minimum guarantee" leads to a reduction in Savings Credit of GBP 0.4, up to the point where they are no longer entitled to Savings Credit.

The qualifying age for Pension Credit increased to 66 for both men and women in October 2020. The savings credit element of the scheme is not available to those who reached State Pension age on or after 6 April 2016 (i.e. the same cohort that qualify for the new State Pension).

Variant careers

Early retirement

It is not possible to claim a State Pension early. Voluntary pension benefits can be claimed from the age allowed by the scheme.

Late retirement

Deferral of the State Pension has always been possible in order to earn extra State Pension increments. This extra State Pension is paid on top of the normal State Pension when a person eventually claims for the first time or claims again.

The amount of extra money a person gets depends on how long they put off claiming their State Pension.

For those reaching State Pension age before 6 April 2016, they may choose one of the following options:

- A higher weekly state pension for life (if the State Pension is deferred for at least 5 weeks). From 6 April 2005, deferral of the State Pension earned approximately 10.4% for each year of deferred claim (or one per cent for every five weeks).

- A one-off taxable lump-sum payment (if the State Pension is continuously deferred for at least one year). The lump sum is made up of the State Pension foregone during the deferral period plus interest which is guaranteed to be at least two percentage points above the (Bank of England) base rate.

The choice has to be made when the State Pension is eventually claimed.

For those who reach State Pension age from 6 April 2016 onwards, it will not be possible to take a lump-sum payment. To receive a higher weekly State Pension for life, the State Pension will need to be deferred for at least nine weeks. Deferral of the new State Pension earns approximately 5.8% for each year of deferred claim (or one per cent for every nine weeks).

Childcare

National Insurance credits for the new State Pension provide protection for periods of childcare. This covers both people not in paid work and those working but earning below the lower earnings limit (LEL) who therefore do not contribute to the system.

Unemployment

Periods of unemployment on insurance or assistance benefits are credited to a person's National Insurance contributions record for the new State Pension.

Self-employed

In the basic pension scheme the benefits do not depend on earnings and the self-employed can expect the same benefits as employees with the same length of the contribution record. The self-employed are assumed not to be covered by the occupational pensions because, by contrast to employees, the self-employed are not auto-enrolled to occupational pensions, and they contributions cannot be matched by employer.

Personal income tax and social security contributions

Taxation of pensioners

No special relief is available for pensioners.

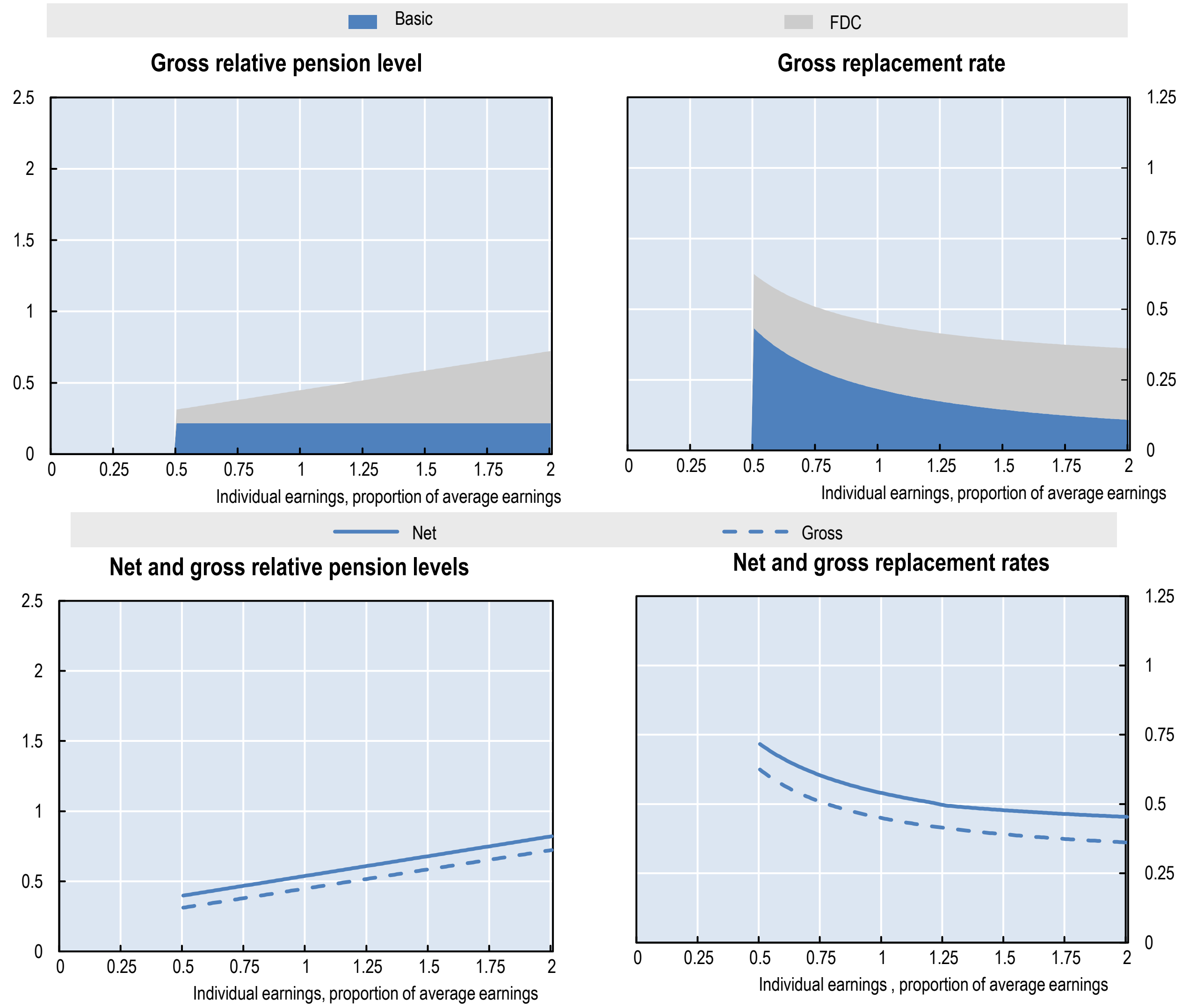
Taxation of pension income

No special relief is available for pension income.

National insurance contributions paid by pensioners

National insurance contributions are not levied on the income of those over State Pension age.

Pension modelling results: United Kingdom in 2065 retirement at age 67



The results in the table below take account of the floor to contributions for the worklplace private pension, which were mistakenly excluded when calculating the results in the main publication

Men	Individual earnings, multiple of average					
Women (where different)	0.5	0.75	1	1.5	2	3
Gross relative pension level	31.2	38.1	44.9	58.6	72.3	99.6
(% average gross earnings)						
Net relative pension level	39.8	46.9	53.9	68.0	82.1	110.3
(% net average earnings)						
Gross replacement rate	62.4	50.8	44.9	39.1	36.1	33.2
(% individual gross earnings)						
Net replacement rate	71.6	60.3	53.9	47.8	45.4	42.7
(% individual net earnings)						
Gross pension wealth	11.6	8.8	7.3	5.9	5.2	4.5
(multiple of individual gross earnings)	*12.9*	*9.7*	*8.2*	*6.6*	*5.8*	*5.0*
Net pension wealth	13.3	10.4	8.8	7.2	6.5	5.8
(multiple of individual net earnings)	*14.8*	*11.6*	*9.8*	*8.0*	*7.3*	*6.4*

Assumptions: Real rate of return 3%, real earnings growth 1.25%, inflation 2%, and real discount rate 2%. All systems are modelled and indexed according to what is legislated. Transitional rules apply where relevant. DC conversion rate equals 90%. Labour market entry occurs at age 22 in 2020. Tax system latest available: 2020.