"Triple lock" increases to the UK State Pension - proposal for a more sustainable approach

International Actuarial Association Joint Section Virtual Colloquium

October 11 - 15, 2021

IAA PBSS section Wednesday 13th October B5 15:40-16:00

Martin Lunnon

UK State Pension system

"Flat-rate" pension payable from State Pension age (SPa)

- Based on payment of National Insurance contributions (NICs) and "credits"
- One pillar in a multi-pillar system – not perhaps the biggest

  Occupational and personal pensions very important
- Means-tested benefit just below flat-rate of State Pension as safety net
- SPa – 66 for all; pre-2010 – 60 for women, 65 for men; further increase expected in mid-late 2020s and perhaps more later
- Different rules for those reaching SPa before and from April 2016

UK State Pension system

New State Pension – those reaching SPa from April 2016

- Flat-rate – currently c £180 a week full-rate

  (= c £9,400 / €10,900 / US$12,750 a year)
- Needs 35 years' contributions/credits for full rate
- No inheritance/derived rights
- Additional payments for those with big rights in pre-2016 system

UK State Pension system

State Pension for those reaching SPa before April 2016

- Flat-rate and earnings-related components
- Flat-rate currently c £120 a week (= c £6,250 / €7,250 / US$8,500 a year)
- Earnings-related component c 20% (capped) earnings but complicated (contracting out!). Could be up to c £12,000 a year
- Earnings-related component gradually becoming flat-rate (more complicated still!)
- Inherited and “derived” rights – protection to women with partial contribution records

UK State Pension system – history of increases since 1970s

- Earnings – or better of earnings and prices
- Prices (RPI)
- Prices but with de facto underpin to avoid low increases
- Earnings
- “Triple lock”
- “Triple lock suspended” (for a year or two?)

An aside – why the UK State Pension system is likely to remain, and remain un-means-tested

Frequent comment by younger (and middle-aged) people – “The State Pension won’t be there when I get old”

Or, the idea that the government should save money by means-testing the State Pension

Responses to these thoughts

- Social contract
- Sustainability
- Remember two key UK features
    - Second pillar – occupational based savings with opt-out
    - Means-tested safety net

Another aside – is the UK State Pension the least generous in Europe

Claim often made – UK State Pensions (£6,000 or £9,400 a year) compared with startling figures for the much higher levels of pension in other EU countries

Misunderstanding of Bismarckian social insurance schemes vs UK's Beveridgean arrangement – ignores UK's generally funded occupational and personal second pillar (such pensions at such a substantial level are rare elsewhere in the EU

UK system quite good at protecting low-paid and those with short careers/broken working patterns

See EU Pension Adequacy Report 2018
https://ec.europa.eu/social/main.jsp?catId=738&langId=en&pubId=8084&furtherPubs=yes

The “triple lock”

Political promise – made by governments since 2010

Best of

- Increase in prices (CPI)
- Increase in earnings (average earnings)
- 2.5%

Legal requirement – increase in earnings, de facto floor 0%

(Social Security Administration Act 1992 s150A – https://www.legislation.gov.uk/ukpga/1992/5/contents)

Triple lock – policy rationale

Avoids pensioners

- Losing out on purchasing power (increases at least in line with prices)
- Losing out compared to workers (increases at least in line with average earnings)
- Getting only a small cash increase

Triple lock – likely effect

- Increases above growth in average earnings in medium- and long-terms.
- Step increases at times of economic “oddness"
- Long-term modelling assumes constant increase = earnings + 0.36% a year (latest “Fiscal sustainability report” published by Office for Budget Responsibility July 2020 – https://obr.uk/fsr/fiscal-sustainability-report-july-2020/).
- Rate of increase above earnings could be rather higher in certain economic scenarios, especially low price and low earnings growth situations – see http://paullewismoney.blogspot.com/2015/10/gad-on-triple-lock.html

How triple lock has operated in the last few years and how the corona-virus pandemic has affected it – projections made about a year ago

Table D.4 – Triple Lock increases (historic and central projection assumptions)

Year of April up-rating	CPI	AWE	Minimum increase	Triple lock	Value of £100 after cumulative Triple lock increases
2016	-0.1%	**2.9%**	2.5%	2.9%	£102.90
2017	1.0%	2.4%	**2.5%**	2.5%	£105.47
2018	**3.0%**	2.2%	2.5%	3.0%	£108.64
2019	2.4%	**2.6%**	2.5%	2.6%	£111.46
2020	1.7%	**3.9%**	2.5%	3.9%	£115.81
2021	0.5%	-1.0%	**2.5%**	2.5%	£118.70
2022[1]	1.4%	**4.1%**	2.5%	4.1%	£123.57
2023[1]	1.6%	2.0%	**2.5%**	2.5%	£126.66
2024[1]	1.8%	2.4%	**2.5%**	2.5%	£129.83
2025[1]	1.9%	**2.8%**	2.5%	2.8%	£133.46

[1] Figures for 2022-2025 up-ratings are projections

Source: UK Government Actuary's Department "Up-rating report" published Jan 2021

https://www.gov.uk/government/publications/report-to-parliament-on-the-2021-re-rating-and-up-rating-orders

How the corona-virus pandemic has affected the triple lock in the most recent years? Situation now (early October 2021)

Table D.4 – Triple Lock increases (historic and central projection assumptions)

Year of April up-rating	CPI	AWE	Minimum increase	Triple lock	Value of £100 after cumulative Triple lock increases
2016	-0.1%	**2.9%**	2.5%	2.9%	£102.90
2017	1.0%	2.4%	**2.5%**	2.5%	£105.47
2018	**3.0%**	2.2%	2.5%	3.0%	£108.64
2019	2.4%	**2.6%**	2.5%	2.6%	£111.46
2020	1.7%	**3.9%**	2.5%	3.9%	£115.81
2021	0.5%	-1.0%	**2.5%**	2.5%	£118.70
2022[1]	c 4%	c 8%	2.5%	c 4%	[illegible]
2023[1]	[illegible]	2.0%	**2.5%**	2.5%	[illegible]
2024[1]	1.8%	2.4% ?	**2.5%**	2.5%	[illegible]
2025[1]	1.9%	**2.8%**	2.5%	2.8%	[illegible]

[1] Figures for 2022-2025 up-ratings are projections

Is this sensible?

Another aside – would abandoning or altering the triple lock hit female or other poor pensioners the hardest? Is it the best solution to helping such poor pensioners?

Yes – female pensioners have lower pensions than men (even for State Pensions, though in time new State Pension may substantially reduce that). Older pensioners (disproportionately female – longevity) are worse off than younger pensioners. See https://www.gov.uk/government/statistics/pensioners-incomes-series-financial-year-2019-to-2020/pensioners-incomes-series-financial-year-2019-to-2020

Better solution than triple lock – focus more help on older pensioners, perhaps by ensuring that all get at least £180 a week (post-April 2016 rate)

Longer-term – reasonably well-off couples, poor single pensioners (especially widow/ers)

Possible solution – some kind of survivors/widow(er)s benefit. Or encourage flexible drawing from funded pensions

Proposal – an alternative way to boost the main rate of the UK State Pension over time

Two questions

- Should we increase the rate of the State Pension relative to earnings over time?
- If so, is the triple lock the best way of doing so?

I say “not certain” and “probably not“

Better – link to size of workforce (a measure of ability to pay for any real increase)