Policy Statement

PENSIONS

A pensions policy for an independent Britain

January 2010

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Introduction

The pensions system, like the welfare state, has developed over decades. The UK Independence Party (UKIP), believes that the pensions system has three purposes: to alleviate poverty in old age, to encourage people to save for their retirement and to reward long serving public sector workers, who until recently had generally earned a lower salary than private sector workers. UKIP feels that the current system is failing to meet these objectives.

The current pension system is flawed. Despite the billions spent every year on pensions, around 2 million British pensioners live below the official poverty line. It is reprehensible that a large number of pensioners face the dreaded "heat or eat" choice as a result of the poverty inflicted upon them by an unfair system. In Britain, one of the world's richest nations, it is totally unacceptable that such levels of poverty and deprivation can be allowed to exist amongst our older people.

Previous governments have hardly helped with the current system. The Conservative party abolished the link to earnings, whilst the succeeding Labour government which succeeded it did nothing to restore this link. In terms of tax reliefs for pension contributions, more than half of this relief accrues to higher rate tax payers, despite the fact they only make up around 15% of the population. UKIP believes that these reliefs, as currently constructed, are badly targeted.

Median full time salaries in the public sector are now 16% higher than in the private sector[1]. There are now nearly eight million people employed in 'Education, Health and Public Administration' – two million more than in 1997 and one-in-four of all UK workers. Most of these schemes are unfunded, and calculations show that a fund of around £1,000 billion would be required to cover the future liabilities if the schemes were funded. This vast sum is equivalent to two-thirds of the UK's entire national GDP.

It has been argued that the need to fund our welfare and pensions system necessitates the encouragement of mass immigration. The argument is that new workers are needed from overseas to support the retired population through tax. This is over simplistic. The ratio that matters is not workers-retired persons, but workers-economically inactive persons (including young children, students, the unemployed and many public sector workers). Furthermore, many immigrants themselves will need a pension one day as well. Thus, mass immigration is not the solution to any pensions crisis.

To that end, the UK Independence Party sets out here to reform the UK pensions system. Our belief is that pensioners have worked hard over a lifetime, and deserve financial security and peace of mind in their later years. Pensions are not like benefits or welfare. Pensions are a right, earned by a lifetime of hard work and contributions to tax and national insurance.

Headlines

Pension fund deficits 'slashed' - BBC 10/11/09
http://news.bbc.co.uk/1/hi/business/8352225.stm

MPs struggle to live on state pension for a week - WalesOnline 9/11/09
http://www.walesonline.co.uk/news/wales-news/2009/11/09/mp-s-struggle-to-live-on-state-pension-for-a-week-91466-25124147/

Pensions crisis to hit millions of workers - Daily Telegraph 23/6/09
http://www.telegraph.co.uk/finance/personalfinance/pensions/5616635/Pensions-crisis-to-hit-millions-of-workers.html

Gold-plated pension schemes threatened by £100bn deficit – Daily Mail 22/12/09
http://www.dailymail.co.uk/news/article-1237566/Black-hole-200-pension-schemes-passes-100bn-time.html

Numbers working past retirement age set to double – Finance Markets 11/11/09
http://www.financemarkets.co.uk/boards/those-working-past-retirement-age-set-to-double-4261.html

Pensioner found dead in council bungalow with no heating, lighting or hot water - This is Staffordshire 18/12/08
http://www.thisisstaffordshire.co.uk/news/pensioner-die-sad-lonely-death/article-557304-detail/article.html

UK elderly fourth poorest in EU 29/7/09
http://news.bbc.co.uk/1/hi/uk/8169859.stm

Pensioner poverty is 'unacceptable' – Daily Mirror 30/7/09
http://www.mirror.co.uk/news/latest/2009/07/30/pensioner-poverty-is-unacceptable-115875-21557837/

UK missing out on £2.7 billion of pension's cash – unbiased.co.uk
http://www.unbiased.co.uk/find-an-independent-financial-adviser/media/press-releases/uk-missing-out-on-2-7-billion-of-pensions-cash-%28consumer%29-07037/

One million fewer Britons in company pension scheme than ten years ago – Daily Telegraph 26/12/09
http://www.telegraph.co.uk/finance/personalfinance/pensions/6895218/One-million-fewer-Britons-in-company-pension-scheme-than-ten-years-ago.html

Council fear £616 million pension deficit - Bury Free Press 1/1/10
http://www.buryfreepress.co.uk/news/County-council-fears-a-616m.5949477.jp

3 Executive summary

3.1 This policy statement looks at the main areas in which the State is involved in old-age provision and suggests how each of these can be radically simplified, so that very few are worse off (within existing expenditure constraints) while at the same time removing many of the pitfalls.

3.2 The main recommendations are:

- To end discriminatory and over complex means testing on pensions, UKIP would roll all existing State pensions, Pensions Credit, the Winter Fuel Allowance into a flat-rate non-means tested, non-contributory and non-taxable "Citizen's Pension" of £130 per week for all pensioners aged 65 and over.

- In order to better target the value of the tax reliefs for pension contributions on low and average earners, to reduce the annual limit for tax-relievable pension contributions to £10,000 gross from £235,000 now and reinstate the dividend tax credit at 20%.

- To allow more flexibility in the use of the final value of a pension fund.

- To scrap the statutory Pension Protection Fund and the National Pensions Savings Scheme as they are costly and counter-productive, and encourage industry wide funds to reduce administration costs.

- To bring the generosity of unfunded public sector final salary pensions back into line with typical pension provision in the private sector to avoid potential liabilities of £1,000 billion.

- To leave the EU to avoid massive liabilities in supporting unfunded EU pensions that would wreck the UK economy (UK has 74% of GDP invested in pensions, Germany just 5.8%, France 5.6%, Italy 3%).

4 Britain's pensioners

4.1 In Britain, the term “pensioner” refers to any man over 65 and any woman over 60, though this is due to change from 2010. Thus, pensioners are the generation born around the time of the Second World War, or even before it. This generation has seen Britain change dramatically over the decades, sometimes for the better, and other times for the worse. For the better, they have seen many diseases eradicated and seen advances in technology and opportunity their own parents could never have imagined. For the worse, they have seen spiralling crime and indecency[2].

4.2 Despite their work, this generation often suffers from huge problems. Pensioner poverty remains unacceptably high, with around 2 million pensioners living below the poverty line[3]. Indeed, despite being the third largest economy in Europe, British pensioners are the fourth poorest in the whole of the EU. Many pensioners are so poor, they face what some campaigners call the "heat or eat" dilemma. That is, they can afford to eat or heat their home, but not do both. Indeed, a large number of pensioners are believed to die every winter for exactly this reason. It has been estimated that this number could be as high as 20,000 per annum, which includes pensioners who die directly of cold, and those who have existing medical conditions aggravated by the cold[4].

5 The current system and its problems

5.1 The total cost of the State pension and other old-age benefits is £75 billion per annum (see appendices), an average of £122 per week for all those over the current pensions age (or £145 per week if the retirement age for men and women were aligned), yet around 40% of pensioners still live below the official poverty threshold because they fail to claim or qualify for various benefits[5].

5.2 The total current cost of the various tax reliefs for pensions contributions and pension funds is over £47 billion per annum or over 8% of GDP[65]. UKIP agrees that saving towards an old age pension should be encouraged, but the reliefs are badly targeted. The total value of the reliefs averages out at £1,000 per taxpayer, but this masks the fact that 55% of the relief accrues to higher rate taxpayers[7], who only make up ten or fifteen per cent of taxpayers.

5.3 Median full time salaries in the public sector are now 16% higher than in the private sector[8]. There are now nearly eight million people employed in ‘Education, Health and Public Administration’[9] – two million more than in 1997 and one-in-four of all UK workers. Most of these schemes are unfunded, and calculations show that a fund of around £1,000 billion (around two-thirds of GDP) would be required to cover the future liabilities if the schemes were funded.

5.4 One of the arguments used to justify immigration is that the UK has an ageing population. This may well be true, but completely overlooks the fact that it is not the ratio of workers-to-pensioners that matters, but the ratio of productive workers-to-everybody else (pensioners, children, students, the unemployed and non-productive public sector workers). Thus mass immigration does not pose a serious solution to the current pensions crisis, and may actually aggravate the situation long term, as immigrant workers age and themselves demand a pension.

5.5 The Basic State Pension ('BSP') accounts for around two-thirds of total cost of age-related benefits paid out (see appendices). It is not means-tested and the maximum pension is covered by the tax-free personal allowance. It is paid out based on the number of years' contributions made, so coverage is poor; despite the upward adjustments for Home Responsibility Protection (and similar predecessor schemes). Women receive, on average, 75% of the BSP while men receive 90%[10]. However, men have to wait five years longer to qualify and have shorter life expectancies after retirement.

5.6 The State Second Pension ('S2P', formerly known as State Earnings Related Pension or 'SERPS') is an average of £13 per week. For those who have 'contracted out' of S2P and invested the rebate privately, the notional value of the pension income generated is an additional £12 per week, i.e. £25 per week in total.

5.7 Pensions Credit (guarantee credit). The pensions credit is supposed to "guarantee" a minimum income of £124 a week for a single pensioner (£189 for a couple)[11]. Around a third of the theoretical entitlement goes unclaimed[12] against a total payout of £6.3 billion. The withdrawal rate is up to 100% of *net* other income or 200% of investment income (the assumed interest/dividend rate is 10% per annum). This is a complete and counterproductive disincentive for those on low incomes to save for retirement.

5.8 Pensions Credit (savings credit). Instead of assuming a lower rate of return on savings or a lower withdrawal rate, there is a parallel Savings Credit, which *rises* with additional savings or other pension income up to a maximum of £19 per week (£26 for a couple).

5.9 It defies belief that the Department of Work and Pensions are supposed to go to all the trouble of running the State Pension system and then over-layering it with the patchy and complex Pensions Credit. Either we wish to link pensions to a lifetime of work/caring (and to allow some people to fall through the cracks) or we should want to guarantee a minimum income.

5.10 As things stand the system achieves neither; even under Lord Turner's proposals (which would see the pensionable age increased, and greater flexibility in public sector workers' pensions), a third of pensioners will still have to apply for means-tested benefits in thirty years' time. More to the point, a single pensioner on the full Basic State Pension of £91 per week plus average S2P of £13[13] receives less than the current Pensions Credit level of £124. A single pensioner on the full State Pension and average S2P plus average contracted out deductions of £25 receives just above the Pensions Credit level.

5.11 Two-thirds of pensioner households receive additional income from a private pension or a former employer's pension scheme[14], and nearly all those households receive an additional pension that puts them well above the Pensions Credit limits. However, there are still several hundred thousand pensioners who have built up a small pension but who are no better off, as they lose up to £1 in Pensions Credit for each £1 of other pension income.

6 The Solution – The Citizen's Pension

6.1 In summary, the current system is shambolic, with a complicated system of form filling, means testing and requirements to apply for benefits and assistance. Many older people find this process demeaning, complicated and some as a result fail to claim everything they are entitled to. This has the effect of worsening their economic situation. The current system clearly needs a radical overhaul.

6.2 UKIP therefore proposes a radical simplification. We feel that every pensioner aged 65 or over, whether single, widowed, married or cohabiting, should have the choice between:

- Continuing to claim their existing BSP/S2P (and various other minor benefits), and;
- Claiming a non-taxable, non-means tested "Citizen's Pension" of at least £130 per week, equivalent to the current Pensions Credit level (plus value of free TV licence and Winter Fuel Allowance). A couple, who are both over 65, would be entitled to at least £260 per week.
- The important difference between the Citizen's Pension and The Pension Credit will be its simplicity. It will not be means-tested and will be paid out at the higher of a) £130 per week; and b) the total of an individual's existing taxpayer funded or public sector pensions (information which the Pensions Service and the various government departments should be able to compile relatively easily), so it will not be reduced if a pensioner (or their spouse or partner) has a private pension or other savings and investment income.

6.3 The basic rules will have to be modified slightly for those who have previously contracted out of National Insurance. The Department for Work and Pensions keeps a separate record of the notional value of those 'contracted out deductions' (the actual pension income may be more or less, of course, depending on investment performance, annuity rates etc). The notional value of contracted out deductions will be deducted from the standard amount of £130 per week (referred to as 'the offset method' by the Pensions Policy Institute[15]).

6.4 There has been some anger over the perception that recent arrivals to the UK are getting the same entitlements as people who have lived here all their lives. The Citizen's Pension will therefore also be based on the length of Citizenship. The amount will be reduced *pro rata* if the claimant has not lived in the UK for forty years prior to retirement.

6.5 This will not apply to UK citizens living abroad. Their contributions made abroad will be counted. The UK has a network of agreements with other countries as to the mutual pension entitlements of expatriates, which may or may not be in need of overhaul, for example, those who retire to some countries have their BSP entitlement frozen whereas those who retire to others continue to see their pensions indexed up. In any even, such pensioners are not entitled to the Pensions Credit and so there is a good argument for excluding them from the number entitled to the Citizen's Pension.

6.6 UKIP agrees that with increasing life expectancy, it is only fair for the State pension age for women to be increased to 65 (the same as for men) by 2010 and for the State pension age to be subsequently increased to 68 by 2046 (increasing, on average by one month each year). We have no objections to the Government's plans[16] in this regard. As explained above, total spending on the State pension and other age-related benefits amounts to £145 per week if averaged out over all pensioners aged 65 or over, but only £122 if averaged out between men aged 65 or over and women aged 60 or over.

6.7 There is an inevitable trade-off between retirement age, the level of the Citizen's Pension and the tax that needs to be raised to fund it. This is a common sense solution on pensions.

6.8 Paying a weekly Citizen's Pension of £130 to the 9.9 million UK residents aged 65 or over would cost, for 2008-09, £67 billion. The total cost would be increased by the following items:

- Existing State pensions being paid to expatriates
- Existing State pension being paid to those whose existing entitlement is already more than £130 per week.

6.9 The following adjustments would reduce the total cost:

- Reductions for those who now live here but have not spent their whole working lives here
- There will be no increase in the cost of pensions for those individuals whose existing taxpayer-funded or public sector pensions already exceed the Citizen's Pension rate.
- Adjustments for Contracted Out Deductions.
- Transitional measures for women aged between 60 (rising to 65 by 2020) and 65.
- The initial cost of the Citizen's Pension would be slightly higher than the current cost of State pensions, but these will quickly be reduced as the State pension age for women approaches 65 in 2010 and the net cost will be far less than the savings identified in UKIP's welfare proposals.

6.10 Besides a welcome simplification, UKIP hope that Citizen's Pensions would ensure a safety net against absolute poverty in old age – in which the Pensions Credit has failed, largely because the forms are complicated and humiliating, as evidenced by the shamefully by the fact that by the Government's own figures, over one third of pensioners do not claim Pensions Credit[17]. It would also introduce certainty to future pension planning and encourage private provision. For lower earners with less than the full BSP/S2P, there is little point making private provision, as for each £1 of *net* private pensions income, the Pensions Credit is reduced by up to £1.

6.11 Under UKIP's flat tax proposals, income tax and Employee's National Insurance will be rolled into a flat tax, and no further entitlements to the BSP or S2P will accrue. Existing accrued entitlements will be frozen and carried forward so that those within a few years of retirement who have built up the right to BSP/S2P of more than £130 (or the future value of the Citizen's Pension) will continue to benefit from past contributions.

7 Detailed proposals – tax relief for pension contributions

7.1 The total cost of the various tax reliefs for personal and employer pension contributions is around £34 billion per annum. The basic reason for giving tax relief for pensions contributions is to help alleviate poverty in old age by encouraging and enabling people to save for their own retirement. The system of reliefs that has developed over the decades appears to have lost sight of these basic aims – 55% of the value of the tax reliefs now accrues to higher rate taxpayers - and the fact that the overall pool of investments in which pension funds and annuity providers can invest is limited.

7.2 There are four ways to decide on the maximum total annual contributions on which tax relief can be claimed:

1. To pluck a figure like £235,000 out of the air, which our current government appears to have done, which clearly can only benefit very high earners
2. To look at the total value of assets into which pension funds can invest (and apportion this between all potential savers, i.e. those currently in employment or self-employment)
3. To look at the total value of assets in which annuity companies can invest to generate the income to pay annuities (and apportion this between all pensioners)
4. To take the total value of the current tax reliefs, and set the upper limit so that the total value of the reliefs would remain constant, assuming that half of all potential savers were making the maximum contribution.

7.3 UKIP concludes that tax relief can be far better focussed on alleviating poverty (rather than allowing already wealthy individuals to become even wealthier) if:

- The upper limit for tax relievable contributions were reduced from £235,000 to £10,000 per annum
- Tax relief were be harmonised at 20% of gross contributions (the same rate at which pensions will be taxed).
- The dividend tax credit of 20% for UK shares owned by pension funds were to be reinstated.

8 Detailed proposals – pension fund regulation

8.1 The Pension Protection Fund was originally intended to cost UK plc's pension funds £150m in 2005, which has already "risen sharply to £675m in 2007-08" and may rise further, depending on future decisions of the EU's European Court of Justice, experts estimate that the cost will rise to £3 or £4 billion[18][17].

8.2 This is a form of disguised and particularly unfair taxation and the Fund should be scrapped as soon as possible. An employer's pension is a private contract and if an employer fails to meet it, he will go bankrupt and vice versa. The taxpayer in general or solvent pension funds in particular should not be made to foot the bill – remembering always the existence of the taxpayer-funded, State-guaranteed Citizen's Pension that UKIP proposes.

8.3 Employer defined benefit schemes (known as ‘final salary schemes’) made sense in the 1950s and 1960s when many people stayed with the same employer for life, but it seems that these schemes are being closed or at least closed to new entrants because people tend to move between jobs more often and because they merely transfer risk away from the employee to the employer. The massive regulatory burden and investment risk have speeded up their demise.

8.4 UKIP does not believe that a government should introduce more regulations to encourage final salary schemes, or prop them up with more fiddly tax breaks. The US government set up a rescue scheme to provide the same protection and the scheme itself now has a deficit of $5.4 billion[19].

8.5 We therefore propose to scrap the Pension Protection Fund, an unfair tax that punishes well-funded schemes for the benefit of insolvent ones and which can be an encouragement for struggling schemes to default.

Protection of employees’ pension funds.

8.6 Keeping annual management charges as low as possible is key to encouraging pension savings. “In the UK, the 1 to 1.5 per cent a year administration charge typically made for a private pension can reduce its final value by 20 to 30 per cent.”[20]. Even for a higher rate taxpayer whose employer pays directly into a fund (thus saving Employer’s and Employee’s National Insurance as well as higher rate tax), takes 25% tax free cash on retirement and only pays basic rate tax on the annuity income, such charges would take away half the value of the tax reliefs. The situation is much worse for smaller savers who make personal contributions and only receive relief at the basic rate of income tax (it is quite possible that the charges wipe out the value of the tax relief).

8.7 Although protective legislation has been put in place since the Maxwell affair, and there was more in the Pension Act 2004, none of the measures would prevent a fraudster doing what Maxwell did. Today here are discussions in pension circles at the moment about the merits of employers pooling investment funds in order to save on administration and regulatory costs.

8.8 This is a sound idea; many schemes on the Continent are set up on an industry basis, for example in Italy employers in the hairdressing industry, instead of each having a small scheme, pool all their funds. Extending that idea over here will offer a greater degree of security of funds and help keep costs down. Contributions would be handed over to a firm of trustees to administer the scheme. Thus the pension funds are divorced from the employer.

The National Pension Savings Scheme

8.9 UKIP opposes the plans to force employers to contribute 3% of an employee’s salary into a pension scheme unless the employee opts out. The Government suggests that employees contribute 4% of salary with “1% tax relief”. The unintended consequences of this must be immediately obvious.

8.10 Economically rational younger people should be paying off student debts, saving up a deposit or paying off their mortgage in priority to saving for retirement and so will choose to opt out. Women with lower earnings need every penny and so will be forced to opt out. A compulsory contribution by employers is tantamount to an additional payroll tax and so will depress long-run headline earnings. The Association of British Insurers has suggested, "the taxpayer might meet some of the set-up costs". Given that the aim of the accounts is to reduce the tax burden on those who opt in, the additional tax burden must be intended to fall on those who opt out. Thus it is quite possible that net incomes of "younger people and women with lower earnings" will suffer a double-hit; they will have less money now; and much less in future.

9 Detailed proposals – lump sums, annuities and tax on pension income

9.1 The rules on annuities have been relaxed over recent years and there are now exemptions from the obligation to commute the accumulated fund to an annuity by a certain age. But broadly speaking, 25% of a personal pension can be taken entirely tax free, or an employer can pay a certain fraction of final salary tax free, and once the fund is converted to an annuity, it is taxable in full.

9.2 UKIP recommends a radical simplification of the various rules by which taking an annuity can be deferred. Once somebody has reached retirement age, they should:

- At any time be allowed to take the 25% tax-free cash (or the corresponding rules for an employer pension)
- Provided they have purchased an annuity providing an income at least equal to the amount of the Citizen's Pension, be able to withdraw some or all of the balance after deduction of the normal rate of tax/NI, (this is no different in principle than if an employer made a lump sum payment to a retiring employee above the tax free limits).

9.3 Superficially, the current income tax rate on personal or employer pensions in payment is 20% (for 2008-09 onwards), the basic rate of tax. On closer inspection, there are a plethora of different tax rates. For example, depending on various upper and lower limits, the Pensions Credit is withdrawn at between 40% and 100% of an individual's additional pension or 25% of additional investment income (the calculations are tortuous – the guidance notes for advisers run to 82 pages; these figures are based on the Pension Service's on-line calculator).

9.4 Another example would be the age-related personal allowance of £9,030 in 2008-09 for a pensioner aged 64 – 74 (£9,180 thereafter). Therefore, for nearly all pensioners, the BSP/S2P and the next two or three thousand pounds of income are – on the face of it – tax-free. Quite what the true effective overall income tax/withdrawal rate is depends on the all the different variables and interactions; in any even the overall effective rate appears to be around 40%, for example, a single pensioner with an annual BSP of £100 has a total income of £6,720 with Pensions Credit. A different single pensioner with the same BSP and £4,030 in private pension income has a total net income of £9,030. In other words, the additional £4,030 gross income equates to additional £2,310 net income.

9.5 If a better off pensioner has income over the 'Income limit' of £21,800, the higher personal allowance is reduced by half the additional income, so a pensioner with income above that level is actually paying 20% on one-and-a-half times the additional income, an effective tax rate of 30% for interest or pension income.

9.6 We believe in simplifying government and taxation for all. UKIP's policy is therefore that all pension or interest income be taxed at a flat 20%. The Citizen's Pension will be deemed to use up the tax-free personal allowance. Taking the example above, a single pensioner with a BSP of £5,000 and £4,030 private pension income would choose the Citizen's Pension of £6,760 per annum. The £4,030 would be taxed at a flat 20%, leaving £3,224, giving a total net income of £9,984, rather more than under the current rules.

9.7 This will of course leave some marginal cases where, because of the quirks, a pensioner's household is worse off under the new rules. Such households would of course be allowed to continue to claim Pensions Credit and pay tax under the old rules. Over time, the number of such cases will become fewer and fewer.

10 Detailed proposals – Other taxes and benefits

10.1 Around 20% of pensioner households live in social housing, and many are entitled to claim Housing Benefit and Council Tax Benefit. UKIP would replace the administrative burden whereby one department at the council demands rent and Council Tax that pensioners cannot afford and another department makes pensioners fill in complicated and intrusive forms.

10.2 UKIP's policy is that local councils should charge pensioners living in social housing a flat weekly amount in the region of £20 per week each (£40 for a couple), or such higher or lower figure as local councils decide.

10.3 Around 80% of pensioner households are owner-occupiers. A typical Council Tax bill is between 10% and 20% of pension income, so this is a far more pressing topic for most pensioner households than income tax. As Adam Smith wrote, taxes should be levied according to ability to pay, and the means and timing of payment of taxation must be convenient to the payer.

11 Fraud, error and administration costs

11.1 Fraud and error in non-means tested benefits such as the State Pension amounts to only around 0.1% of the State Pension paid out[21]. The administration costs are only around half of one percent of the amount paid out. The fraud, error, administration costs – and just as importantly, the level of unclaimed benefits – in means tested benefits, such as the Pensions Credit, Housing Benefit and Council Tax Benefit is much, much higher. UKIP believes means testing to be wrong, as it is undignified and over complex.

11.2 The government has admitted that 1.6 million pensioners are not claiming £2.1 billion in Pensions Credit to which they are entitled[22] (an average of £25 per week each). The Pensions Policy Institute estimate that 18,000 civil servants alone are concerned with administering Pensions Credits and that the Pensions Credit costs ten times as much to administer as the BSP, in other words, the administration costs are at least 5% of the amounts paid out. The cost of fraud and overpayments and administration costs for other means tested benefits (primarily Housing and Council Tax Benefit) are around 5% of benefits actually paid out as well[23].

11.3 UKIP's proposed Citizen's Pension (to replace all other State pensions and benefits listed in Appendix 1) would be cheap to administer, as it is flat rate and non-contributory. The only information required to process a claim is information already known to the Pensions Service, the Department of Work and Pension or the bodies that administer public sector pensions. Thus administration costs and under- and overpayments would be kept very low.

12 Public sector pensions

12.1 As background, it is useful to compare the relative figures for private and public sector state provision:

- There were 23.7 million people working in the private sector and 8 million in the public sector in mid-2008[24].

- The total assets of the top 2,700 UK pension funds are around £880 billion[25] (the total liabilities are rather more than this).

- The Government are deliberately understating the liabilities of unfunded Public Sector pensions schemes. As at March 2005, the government estimated the liabilities (the 'discounted net present value') of accrued public sector pensions - which in future cash terms will amount to around £3,762 billion - at £530 bn. Using more realistic assumptions, Neil Record[26] calculated the liabilities to be at £1,025 billion, which is now widely accepted as the best estimate[27].

- Around 15% of workers in the private sector are in an employer pension scheme, as against 90% of public sector workers who are in a final salary scheme[28]. There were a further 8.9 million people (28% of all employees and self-employed) making average contributions of £2,200 to personal or stakeholder pensions schemes. These statistics overlap, as some private employers and public sector workers make contributions to personal or stakeholder schemes.

- Unfunded public sector pension promises add around one-third to the official cost of public sector pay. In other words, if a private sector employer made equally generous promises, the employer contribution to a money purchase pension scheme would be an additional one-third of gross salary.

- "Nearly all government employees receive a final salary scheme, which is exceptionally attractive because it guarantees an income. This is typically around two-thirds of workers' earnings on retirement"[29]. "Public sector workers are receiving £210 more per week than their private sector counterparts on average, mostly due to their generous taxpayer-funded pension schemes"[30].

- "The percentage difference between the median level of full-time earnings in the public sector (£539 per week) and the private sector (£465 per week) widened [to 16%] over the year to April 2009 …"[31]

- Early retirement in the private sector accounts for less than 20% of all retirements. The incidence of early retirement in the public sector between 1995 and 2000 as a percentage of all retirements was: Fire service 68%; Police 49%; Local government 39%; Teachers 25%; NHS 23%; Civil Service 22%; and Armed forces 6%. This is despite the fact that the retirement age for most public sector workers is only 60. This infers that either we are employing sickly public servants, the jobs are too "stressful" or that claims are being processed without proper scrutiny.[32]

- The number of public sector workers has increased from around 6 million in 1997 to around 8 million in 2008[33]. The number of workers traditionally identified as 'public sector' (i.e. nurses, doctors, police, prison officers, teachers, armed forces, HM Revenue & Customs and Department of Work and Pensions) has increased from around 1.5 million to around 1.8 million, so by deduction the number of non-core public sector employees has risen from 4.5 million to 6.2 million. The previous Conservative government was far from being a 'small government' so it must be clear that many of these jobs are not adding – and in many cases destroying - value.

12.2 UKIP has a number of possible proposals it will examine to rectify this imbalance. For example, it may be necessary to reduce the number of non-core public sector workers back to 1997 levels and beyond. Also, one could increase the retirement age for members of all public sector pension schemes to 65 (a plan abandoned by the current Labour government in the face of union pressure in 2005). There could be better policing of early retirement due to ill health in the public sector to bring it in line with the private sector.

12.3 There also needs to be proper accounting for public sector pensions liabilities. Although this will not 'solve' the issue, it will at least highlight it. A reasonable suggestion is that public sector pension schemes liabilities be calculated under normal accounting standards and accounted for as such in public sector accounts. This would prevent a future government hiding the cost of current promises.

12.4 There is also a need to reduce the differential between public sector and private sector wages. Converting unfunded final salary schemes into money-purchase schemes, increasing gross salaries where appropriate and allowing public sector employees the choice of taking it as salary or paying it into a funded pension scheme.

12.5 The combined impact of these various measures would be to halve the current cost of public sector pensions and bring it into line with the typical pension entitlement of private sector workers. This is equivalent to a tax cut of between £500 and £1,000 for every private sector employee.

13 The European Union ("EU") nightmare

13.1 The problems we have in the UK are magnified elsewhere in the EU. Most of their private sector schemes are, in the main, unfunded. The UK has approx 74.7% of GDP invested in pensions against 5.8% in Germany, 5.6% in France and only 3% in Italy. These are massive shortfalls in any language.

13.2 This is also a huge problem for the UK. The House Of Commons Select Social Security Committee on "Unfunded Pension Liabilities in the EU" in 1996 stated "The UK's current National Debt is equivalent to about £5,000 for every man woman and child in the country. If we add on the burden of our unfunded pension liabilities the sum would increase to approx £9,000 per person. If we make a further addition for the liabilities of unfunded pensions in the rest of the EU then the per capita figure for the National Debt would exceed £30,000. The adoption of a single currency would entail the adoption of a single balance sheet, but the extent of unfunded pension liabilities in certain of our partner countries casts serious doubt upon the long term sustainability of their finances".

It is becoming ever more likely that the UK would be asked to bail out other Member States: "Although Britain is not in the eurozone - and despite the fact that many of Greece's problems arise from it having joined the single currency - the UK could be forced into part-funding a bailout under the EU treaty if a majority of other members vote for it. A Treasury source would not comment on whether any official calculations have been made regarding Britain's potential exposure. But with the Athens government expected to borrow £48billion this year, any rescue would be likely to relate to that figure. If contributions were based on a share of EU gross domestic product, then the UK, with about 15 per cent, could face a demand for more than £7billion."[34]

13.3 "As the UK's outstanding public pension liabilities are substantially below those of other EU members, There would be a real risk that if the UK joined a single currency British Taxpayers could be called upon to help finance the 'pay as you go' pension obligations of the EMU members, or suffer the consequences of being tied to interest rates on the single currency that were forced upwards by the market pressures of financing certain countries' inherited pension commitments"

13.4 As a member of the EU we cannot institute changes to avoid the crisis facing the rest of the EU. The size of the problem and its costs to the taxpayer, along with the burden of the EU's social legislation will reduce the efficiency of the EU economy and its chances of competing in a world economy that now includes the likes of China and India with their low wage costs and developing home markets.

13.5 The Institute of Directors in a paper published in 2002 put the cost of full integration and monetary union, including unfunded EU pension costs, at £168 billion. If we again put this in terms of National Debt per man woman and child: the current liability is now £9,100, (an increase of 82% since Gordon Brown took over the reins), adding to the UK's latent liabilities for unfunded public sector pensions promises and Private Finance Initiatives, gives a liability per man, woman and child of something in the region of £20,000 each. Adding the EU's liabilities will mean a National Debt figure per head of population of £71,400. In short, thanks to EU membership, to balance the books, our Chancellor will have to slash public spending in other areas or increase taxes to over 60% of GDP.

13.6 The solution to this particular pension problem is simple – the UK has to withdraw from the EU. Inside the EU we face the destruction of our economy, severe poverty for our pensioners and the rest of us will not have the means to save for our own pensions. It is imperative, to avoid being sucked down into the EU's pensions nightmare.

13.7 Outside of the EU we can then address our own pension problems, which are small by comparison. If we leave the EU, we can start by reducing the burden to industry that EU regulation costs us. The government's Better Regulation Taskforce reported in 2005 that EU regulations cost UK industry around one-tenth of GDP, or over £100 billion per annum[33]. If we can strip out just one-third of this cost from our economy then we are on the way to sorting out our pension problems and finding the additional resources needed to meet those obligations.

Appendix 1 Current State pensions spending

1. The Department of Work and Pensions' forecasts for 2008-09 is as follows (Table 3, http://www.dwp.gov.uk/asd/asd4/medium_term.asp)

	£ millions
Basic State Pension (excl. Category D)	49,927
SERPS and S2P	11,345
Christmas Bonus - contribution-based	129
Widows' and Bereavement benefits	672
Basic State Pension (Category D)	40
Non-contributory Christmas Bonus	21
Winter Fuel Payments	2,664
Over 75 TV Licence	528
Pension Credit (guarantee credit)	6,326
Pension Credit (savings credit)	1,179
Total (Great Britain)	72,831
Add 3% for Northern Ireland	2,185
Total (UK)	75,016

2. The current cost of pensions in payment to former public sector workers is estimated at 1.5% of GDP by HM Treasury, set to rise by a third over the next four decades, this equates to an annual current cost of £22 billion.

Appendix 2 Tax relief for pension contributions

Corporation tax/income tax relief

Per HMRC Table 7.9, the cost of corporation/income tax relief on contributions for 2006-07 was £22.3 billion and the cost of the exemption for investment income of pension funds was £5.1 billion.

The comparable figures for 2008-09 are £24 billion and £5.5 billion in 2008-09.

National Insurance ('NIC') reliefs

Per HMRC Table 1.5, the cost exemption from NIC on contributions to pensions schemes was £8.3 billion for 2007-08. The £8.3 bn can be split between employer's and employee's NIC in the ratio 12.8% to 11%. UKIP would phase out Employer's NIC, so the net cost of the relief would equate to £6.9 billion in 2008-09.

Contracted out rebates cost £10 billion. Employer rebates are 3.5% and employee rebates are 1.6% of salary. Splitting £10 billion between employer and employee in the ratio 3.5% to 1.6%, suggests that contracting rebates will £3.3 billion in 2008-09.

The total cost of the NIC reliefs is around £10 billion for 2008-09.

Income tax on pensions in payment

Per HMRC Table 7.9 for 2007-08, income tax paid on pensions in payment was £10.2 billion, indexed up to £10.6 for 2008-09.

<u>A reasonable upper limit for tax relief on annual pension contributions</u>

Pension funds invest in UK quoted shares and commercial property. The total value of UK quoted shares (as at mid-2008) was £1,800 billion. The total value of UK commercial property not already owned by quoted companies can be estimated at £200 billion, total value £2,000 billion. Assuming that half are owned from overseas, by insurance company or wealthy families, and that 30 million taxpayers all invest the same amount annually, the average amount in each personal fund would be £30,000, i.e. starting with nil and retiring when the fund is £60,000. Assuming that pensioners build up this fund in the twenty years leading up to retirement, the required annual contribution would be £3,000 (ignoring compounding).

Annuity companies invest primarily in UK government bonds (‘gilts’) to enable them to match interest income with annuities that they pay out. The UK’s Public Sector Net Debt was £529 billion at the end of 2007-08. The total interest paid by the government was £30 billion. If UK annuity providers owned all gilts, and all 9.9 million currently aged 65 or over, the average payout per pensioner would be in the order of £60 per week. Assuming current annuity rates, to produce an annuity income of £60 per week, each person retiring at age 65 would require a fund of £65,000 after having taken 25% tax-free cash. To build up such a fund would require annual contributions of £4,000 over a twenty-year period (ignoring compounding).

The total value of tax reliefs for pensions contributions is £34 billion per annum. Assuming that taxpayers only contribute for the second half their working lives (once they have repaid student loans and made inroads into the mortgage), the relief would be around £2,000 per taxpayer per annum. Further assuming that the rate of tax relief were harmonised at 20% for all taxpayers – the same as the rate that is charged on pensions in payment – the maximum relievable contributions would be £10,000 per annum.

UKIP therefore recommends that the upper limit for tax relievable contributions be reduced to £10,000. Of course, only a minority of taxpayers can afford to pay that much into a scheme so the cost of the tax relief would be far less than £34 billion per annum, so to further encourage pension saving, and to level up the playing field between different types of assets in which pension funds can invest, UKIP would also reinstate the dividend tax credit. The total value of tax relief for these two measures would be roughly equal to the value of existing tax breaks, but ensure that more of the benefits accrue more to low and average earners.

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