These notes refer to the Welfare Reform and Pensions Act 1999 (c.30) which received Royal Assent on 11 November 1999

WELFARE REFORM AND PENSIONS ACT 1999

EXPLANATORY NOTES

OVERVIEW

Stakeholder Pension Schemes

Background

The UK pension system is a partnership between the State (providing the basic state pension, the State Earnings Related Pension Scheme – SERPS – and income-related benefits for pensioners); employers (providing occupational pension schemes) and private pension providers (providing personal pensions).

Today's pension system is composed of three tiers:

the first tier is the basic state pension;

the second tier is a mix of state and mainly private provision which are additional to the basic state pension (this tier includes SERPS, occupational and personal pensions); and

the third tier comprises other voluntary private provision.

People are already compelled to save towards a pension. All employees and self-employed people, except the very lowest paid, must pay National Insurance contributions. These give entitlement to basic state pension. In addition, employees have to pay towards a second-tier pension – SERPS – unless they opt out and make their own provision (contracting out). If people are contracted out of SERPS into a private scheme their National Insurance contributions are reduced or rebated to reflect the value of SERPS foregone.

The minimum that must be paid to a second pension is an average of about 4.6% of earnings – 1.6% from employees and employers pay 3% on top. While employees are required to contribute to a second pension, self-employed people are not. The only second pension choice for them is a personal pension, but many self-employed people make some provision for their retirement through other savings vehicles and investments.

Of 35 million people of working age in Great Britain, some 10.5 million are in occupational schemes, around 10 million personal pensions are held and over 7 million belong to SERPS.

Second pension schemes are not available to everyone. Occupational pension schemes are not an option for the 35% of employees whose employers do not offer a scheme, nor for the self-employed. Personal pensions can be less accessible for some people, particularly the lower paid and those who change jobs frequently.

The Government's detailed proposals for pensions reform were set out in the consultation paper *A new contract for welfare: PARTNERSHIP IN PENSIONS* (Cm 4179), published in December 1998.

The consultation paper proposed a new insurance contract for pensions with three main elements:

a guaranteed minimum income in retirement for all, increased year by year as resources allow (this does not require primary legislation). Over the longer term the aim is that this should rise in line with earnings;

reforming SERPS through the introduction of the State Second Pension. This will boost the pensions of low earners, carers and certain disabled people (it is proposed that this will be introduced by legislation in the 1999/2000 session of Parliament);

new, accessible, stakeholder pension schemes. The consultation paper proposed that:

stakeholder pension schemes should be open to everyone but will be targeted at those earning £9,000 – £20,000 and not in an occupational scheme;

there would be a simpler tax regime, allowing up to £3,600 to be paid into schemes each year;

employers who do not already offer an occupational scheme should identify a stakeholder pension scheme and facilitate access to it for their employees; and

stakeholder pension schemes should be set up with an approved governance structure, meet minimum standards and be required to register.

The Government has now legislated to provide the necessary legislative framework for stakeholder pension schemes.

The measures in the Act

The measures in this Act that relate to stakeholder pension schemes are contained in Part I, sections 1 to 8.

The provisions in the Act create a statutory framework for stakeholder pension schemes. There has been further consultation on the detailed aspects of the framework. It is likely that the framework will require adaptation as the schemes evolve. In order to provide this flexibility, many matters of detail will be set out later in secondary legislation.