PENSIONS ACT 2004

EXPLANATORY NOTES

COMMENTARY ON SECTIONS

Part 8 – State Pensions

Retirement Pensions

Summary

1180. Retirement pension is paid to people who have reached pensionable age (currently 60 for women and 65 for men) provided they have made a claim for it. During their working life, they have to have paid, been treated as paid or have been credited as having paid, National Insurance contributions. The amount of retirement pension depends on the number of contributions they have built up.

1181. People must either:

- have one qualifying year since 6th April 1975 which is derived from the payment of Class 1, 2 or 3 National Insurance contributions or from Class 1 contributions treated as paid; or
- have paid 50 flat-rate contributions at any time before 6th April 1975.
- 1182. To get a full rate basic retirement pension, people must have qualifying years for about 90% of the years in their working life. To get a minimum basic retirement pension (25% of the full amount), people normally need 10 or 11 qualifying years.
- 1183. Prior to April 2000, employees started paying National Insurance contributions once their earnings reached the Lower Earnings Limit. From April 2000, a new employees' primary threshold was introduced as the point from which employees start to pay contributions. This is set at a higher amount than the Lower Earnings Limit. As a result, employees who earn between the Lower Earnings Limit and the employees' primary threshold no longer pay National Insurance contributions but will be treated as if they have paid them. This means they will continue to build up entitlement to contributory benefits such as retirement pensions, even though they are not paying National Insurance contributions.

Working life

- 1184. A person's working life is the period over which they have to meet the contribution conditions for basic retirement pension. A working life is normally:
 - 49 years for men;
 - 44 years for women born on or before 5/10/1950;
 - 45 years for women born on 6/10/1950 or any subsequent day through to and including 5/10/1951;

- 46 years for women born on 6/10/1951 or any subsequent day through to and including 5/10/1952;
- 47 years for women born on 6/10/1952 or any subsequent day through to and including 5/10/1953;
- 48 years for women born on 6/10/1953 or any subsequent day through to and including 5/10/1954;
- 49 years for women born on 6/10/1954 or later.
- A working life is counted from the start of the tax year in which a person reaches the 1185. age of 16 to the end of the tax year before the one in which they reach pensionable age.

Qualifying year

A qualifying year for basic retirement pension is a tax year in which a person receives (or is treated as having received) qualifying earnings of at least 52 times the Lower Earnings Limit for that year.

Oualifying earnings

Earnings from Class 1 employment

Earnings on which full-rate Class 1 contributions have been paid or are treated as having been paid count as qualifying earnings. Earnings of married women and widows with reduced liability do not count as qualifying earnings.

Class 2 and Class 3 contributions

Each Class 2 or Class 3 contribution counts as one week's earnings at the Lower Earnings Limit.

Credit of earnings

In certain circumstances a person may be credited with earnings to help them get a retirement pension if they do not have enough earnings in a tax year to reach the level needed to make it a qualifying year. Men with no liability to pay Class 1 or Class 2 contributions may be credited automatically for the tax years in which they reach 60 and the four succeeding years. From 6th April 2010 this arrangement will be extended to women. Young people can get credits for the tax year in which they reach age 16 and the two following years. There are conditions attached to the receipt of credits and the availability of a credit does not mean a person does not have to pay National Insurance contributions if their earnings exceed the employees' primary threshold. Earnings are not credited to married women who have a reduced contribution liability. Flat-rate contributions paid or credited before 6^{th} April 1975

Any flat-rate contributions paid by or credited before 6th April 1975 are converted into a number of qualifying years by dividing the total number by 50 and rounding up what is left over to the next whole number. However, the number of qualifying years calculated in this way cannot be more than the number of years in a working life up to April 1975.

Classes of National Insurance contributions

- There are six classes of National Insurance contributions only three count towards qualifying years for retirement pensions:
 - Class 1 paid by employed earners and their employers. Employees pay these if they work for an employer and earn more than the employees' primary threshold. The employer also pays National Insurance contributions for the employee if they earn more than the employers' primary threshold. There is no upper limit on the employer's National Insurance contributions. Some married women and widows can still pay their National Insurance contributions at a reduced rate.

- Class 2 paid by self-employed people. Paid at a flat-rate.
- Class 3 voluntary contributions which may be paid to protect a person's National Insurance record in some circumstances. Paid at a flat rate. Class 3 contributions can be paid for previous years to enable someone either to qualify for a basic retirement pension at the minimum rate or to increase the rate of the basic retirement pension for which they have qualified. Any arrears of contributions paid after pensionable age cannot normally count for payment of retirement pension from a date earlier than the day on which the contributions were paid. Married women and widows cannot pay Class 3 contributions for any tax year in which they had reduced rate liability for the whole year.

Categories of contributory retirement pension

- 1192. There are two categories of contributory retirement pension (either or both of which may be payable):
 - Category A; and
 - · Category B.

Category A pensions

- 1193. A Category A retirement pension consists of two parts:
 - basic retirement pension dependent on the number of qualifying years in a person's working life;
 - additional retirement pension dependent on a person's earnings, or deemed earnings in their working life, since April 1978.

1194. It is paid to:

- anyone who can satisfy the entitlement conditions;
- anyone reaching pensionable age after 5th April 1979 by using qualifying years of their former spouse for a basic retirement pension only;
- a woman who reached pensionable age before 6th April 1979 by using the qualifying years of her former husband for a basic retirement pension only;
- a widow or widower entitled to long-term incapacity benefit under prescribed circumstances.
- 1195. In order to receive a Category A pension, a person has to have:
 - reached pensionable age;
 - satisfied the conditions for basic retirement pension (or additional retirement pension) or both; and
 - made a claim for retirement pension.

Category B pensions

1196. A Category B retirement pension can consist of a basic retirement pension; or an additional retirement pension; or both. It is payable by virtue of a spouse's qualifying years and earnings. It is paid to: married women; widows; widowers. In the case of a married woman a Category B pension consists of 60% of the spouse's basic retirement pension. In the case of a widow or widower, a Category B pension may consist of a basic retirement pension of up to 100% of the spouse's retirement pension (it may be combined with any Category A pension of the person's own entitlement up to 100% of

a full retirement pension payable to a single person). It may, with certain exceptions, also consist of half of a deceased spouse's additional retirement pension.

Entitlement to more than one pension

Section 296: Persons entitled to more than one Category B retirement pension

- 1197. This section allows people who are entitled to more than one retirement pension (whether of the same category or not) to notify the Secretary of State in writing as to which one of those retirement pensions they wish to receive. Where such notification is received, that person shall be entitled to the retirement pension he has said he wishes to receive in respect of any week commencing after the date of the notice. In default of such notification, that person shall be entitled to whichever retirement pension is from time to time the most favourable to him.
- 1198. Upon Royal Assent, this section amended section 43(3) of the Social Security Contributions and Benefits Act 1992 (which concerns persons entitled to more than one retirement pension). Contributory benefits legislation was consolidated by that Act and although section 43 enabled a person to choose when there is entitlement to two retirement pensions of a different category, it did not do so where a person is entitled to more than one retirement pension of the same category. This mainly affects widows already entitled to a Category B retirement pension who then remarry. The amendment provides that where a person is entitled to more than one Category B retirement pension they can notify the Secretary of State in writing as to which of the Category B retirement pensions they wish to receive. In the event of no such notice, they will be entitled to the one which is most favourable to them. The Department for Work and Pensions made extra-statutory payments in these cases in line with the policy intention.

Deferral of state pension

Section 297: Deferral of retirement pensions and shared additional pensions

The current position

- 1199. A person is entitled to retirement pension from age 60 for a woman and age 65 for a man, providing he makes a claim for it. If a person does not claim his pension from that date he will not receive any pension for the period between pension age and the date of claim. He will instead qualify for an increase to his weekly pension from the point at which he does claim.
- 1200. A person may also be eligible for increments through electing to cancel his entitlement to retirement pension. For example, having drawn his pension at age 65, a man may choose to cancel his entitlement at age 66. A person may cancel his entitlement in this way once only. This means there are in effect two possible opportunities to earn increments the first, by not claiming on reaching pensionable age; the second, by electing to cancel entitlement after claiming.
- 1201. The amount of the increase is calculated using a formula which results in an increase, or "increment", of ¹/7th of 1% of the weekly pension as at the date of claim, for each "incremental period" (equivalent to a week) in the deferment period. Increments of less than 1% cannot be awarded; therefore to qualify for an increase a person must defer claiming for at least seven weeks. The incremental rate is currently equivalent to approximately 7.4% of the weekly rate for each full year deferred. For example:
 - total number of weeks deferred = 52
 - weekly pension (basic plus additional) at date of claim = £90
 - amount of increase = $^{1}/7 \times ^{90}/100 \times 52 = £6.69$
 - total weekly pension = £96.69

- 1202. Increments may normally be earned for a maximum of five years, and may be accrued on all components of the contributory state retirement pension i.e. Category A and B pensions and Graduated Retirement Benefit (the predecessor to the present earnings-related additional pension component of the state pension scheme). Increments may also be earned by deferring the shared additional pension, and Guaranteed Minimum Pension.
- 1203. It is not possible to defer only part of the pension, for example, a person cannot decide to claim just his basic pension while deferring his additional pension (i.e. the pension derived from the State Earnings Related Pension Scheme (SERPS) or the State Second Pension).

Married couples

- 1204. If a married man defers his Category A pension, his wife cannot claim a Category B pension based on his contributions until such time as he claims his pension. However, increments will accrue on both. Similarly, if he claims his pension but later decides to give it up to earn increments, his wife's entitlement to Category B pension will also be cancelled for the same period (subject to her consent) and increments earned on it.
- 1205. If a woman is entitled to her own Category A pension, she can claim or defer it without reference to whether her spouse is claiming his pension. However, in cases where her Category A pension could be increased by virtue of her husband's contributions and that increase is deferred because he is not claiming his pension, no increments would be payable unless she deferred her own pension as well as the increase.
- 1206. A woman who has attained state pension age and claimed her pension will be entitled to increments earned by her deceased husband provided they were married at the time he died, and she does not remarry before reaching state pension age. The inheritable proportion depends on which pension component the increments relate to. Broadly, she will inherit 100% of increments earned on the basic Category A pension, and between 50% and 100% of increments on the additional (earnings-related) pension component, depending on what percentage of the additional pension itself she is entitled to. In addition, one-half of increments on Graduated Retirement Benefit are inheritable.
- 1207. Until April 2010, when equalisation of state pension age for men and women begins to be phased in, only a widowed man is able to qualify for a Category B retirement pension on the basis of his late wife's contributions. Similarly, a widower may only inherit increments earned by his late wife where he himself was over pension age at the time of her death.

Changes to deferment provisions introduced by the Pensions Act 1995

1208. The 1995 Act removed the five-year limit on deferral and changed the weekly rate of increment accrual from ¹/7th of 1% to ¹/5th of 1% with effect from April 2010. The new incremental rate, equivalent to an annual incremental rate of 10.4%, effectively reduces the minimum qualification period to five weeks through the "one per cent" rule.

New provisions

- 1209. In Chapter 6 of the 2002 Green Paper: Simplicity, security and choice: Working and saving for retirement (Cm 5677) the Government included proposals for amending the arrangements for those who defer their state pension, by:
 - bringing forward to 2006 the changes due to be introduced in 2010 (increasing the incremental rate, and abolishing the time limits); and

¹ Since December 2000, it has been possible for the additional pension component of the state pension scheme to be shared as part of a divorce settlement. "Shared additional pension" is the term used for the weekly pension derived from the cash equivalent transfer value of a former spouse's state additional pension.

² Before 1997, salary-related occupational pension schemes could contract their members out of the State Earnings Related Pension Schemes (SERPS) by underpinning their benefits with a Guaranteed Minimum Pension which broadly reflected the pension which they would otherwise have built up in SERPS.

- introducing the choice of a taxable lump sum payment as an alternative to weekly increments for life.
- 1210. There is no change planned to the rule on electing to cancel entitlement as now, a person will be able to do this once only.
- 1211. The intention is now to advance the commencement date of the deferral changes to April 2005.

Increments and removal of time limits

1212. Section 297 amends the Pensions Act 1995 to bring forward the commencement date of the 2010 changes to April 2005. No other substantive changes to the structure or calculation of increments are made.

The lump sum – general conditions

1213. The lump sum will be an option only after a person has deferred for at least 12 months (in contrast to increments, which, following the change in accrual rate, will be payable after five weeks' deferment). However, as with increments, there will be no upper limit on the length of time a person may defer and accrue a lump sum.

Calculation

1214. The lump sum will be based on the pension a person would have been entitled to had they not deferred, plus a rate of return that will be applied weekly and compounded. The pension forgone will be calculated at the rate that would have been applicable in each week (or "accrual period") for which the person defers.

Married couples and provisions for widows/ widowers

- 1215. Both members of a married couple may defer their pension entitlement, either by deferring their own individual Category A pension, or as a consequence of the spouse, from whose contributions the other partner's pension is derived, deferring his. Each member of the couple will have the choice of either increments or (providing the deferment period is at least 12 months) a lump sum, in respect of their deferred pension. So, for example, a woman may prefer an increase to her weekly pension, while her husband elects to receive a lump sum.
- 1216. If a deferrer dies before claiming it is intended that his surviving spouse will be able to choose to "inherit" either a lump sum or increments based on the deceased's deferred entitlement (subject to provisions which restrict this right in respect of deferred pension based on the survivor's own contributions). This choice will only be available if the person had deferred for at least 12 months. In all other respects, the conditions for "inheriting" a lump sum will be the same as for inheriting increments, that is, that the survivor was married to the deceased at the time of death, has attained state pension age and has claimed their own pension (and has not remarried before claiming their pension).
- 1217. Should the death occur before the spouse has attained state pension age, the lump sum as nominally accrued at the date of the deferrer's death will be increased annually in order to broadly maintain its value in line with prices up to the point at which the surviving spouse claims his or her pension. The value of increments earned by a deceased partner is currently protected in a similar way.
- 1218. The calculation of the lump sum for survivors will reflect the proportion of increments that can be inherited; that is, 100% of the lump sum derived from the basic Category A pension, a proportion of the lump sum derived from the additional pension and one-half from deferred Graduated Retirement benefit.
- 1219. In order to maintain consistency with the existing rule relating to the inheritability of increments, before April 2010 a widower's entitlement to an inheritable lump sum will be restricted to cases where the widower is himself over pension age at the time his wife dies.

Provisions of section 297

- 1220. Subsection (1) substitutes section 55 of the Social Security Contributions and Benefits Act 1992 to reflect the introduction of the choice between a lump sum and increments in Schedule 5.
- 1221. The substituted section 55(3) replicates the current section 55(2) and defines when a person's entitlement to their Category A or B pension is deemed to be deferred, that is,
 - if they have not made a claim for their pension (but otherwise would meet the entitlement conditions, i.e. they have attained pensionable age, satisfied the relevant contribution conditions etc), or
 - where entitlement to a Category B pension is derived from the spouse's contributions, if the spouse has not made a claim for his pension, or
 - where the person has chosen to cancel their entitlement under section 54 of the Contributions and Benefits Act.
- 1222. Subsection (2) substitutes section 55C of that Act, which makes provision for increments where shared additional pension is deferred. The new section 55C(1) and (2) introduce a new Schedule 5A which provides for increments or a lump sum to be accrued on deferred shared additional pension (see commentary on Schedule 11 to this Act for the detailed explanation of these provisions).
- 1223. Section 55C(3) replicates the current wording of section 55C(1) which defines when entitlement to a shared additional pension is deferred (that is, where entitlement to Category A or B retirement pension is deferred and the person is not entitled to shared additional pension only because they have not made a claim for it).
- 1224. Subsection (3) amends Schedule 4 to the Pensions Act 1995 so as to bring forward from 2010 to 2005 the operative date for the increase in the rate at which increments accrue where a person defers their entitlement to a state retirement pension or a shared additional pension. This subsection also removes the time limits which currently operate to restrict the period over which a person may accrue increments by deferring their retirement pension.
- 1225. Subsection (4) introduces Schedule 11 to this Act which amends Schedule 5 to the Contributions and Benefits Act 1992 and related enactments and makes transitional provisions.

Schedule 11: Deferral of retirement pensions and shared additional pensions

- 1226. Paragraph 4 inserts a new paragraph A1 at the beginning of Schedule 5 to the Social Security Contributions and Benefits Act 1992. This requires a person who has deferred their Category A or B pension for at least 12 months to choose between increments or a lump sum when they claim their pension. As this choice is not available for those who defer for shorter periods, this provision also effectively sets a minimum qualification period of 12 months for the lump sum.
- 1227. Regulations made under this paragraph will prescribe how the election is to be made and the period within which it must be made. If no choice is made within the prescribed period however, a person will be deemed to have chosen the lump sum (paragraph A1(2)). In other areas of social security legislation where potential entitlement to more than one benefit exists, the Secretary of State has the power to make the decision which is most advantageous for the claimant. In this instance, the Department recognise that for many people, a weekly increase to their pension would, over time, be financially more beneficial; however the lump sum is the "safe" alternative, as it carries no actuarial risk.
- 1228. Regulations made under paragraph A1(3) may provide for a limited "cooling-off" period, during which a person may change their original election, or deemed election.

- 1229. Paragraph A1(4) provides that where a person's deferred pension includes an increase under paragraphs 5 to 6 of Schedule 5 in respect of increments inherited from a deceased spouse who had deferred a Guaranteed Minimum Pension (GMP), he or she is unable to choose between increments and a lump sum for that component of their deferred pension. The intention is that only increments for that element may be awarded, because pension schemes will not be required to change their rules to offer lump sums as an alternative to increments for deferred GMPs.
- 1230. *Paragraph 5* substitutes paragraph 1 of Schedule 5. The new paragraph 1(1) provides that increments will be added to the pension where the person has either deferred for less than 12 months or has deferred for longer but has chosen increments rather than the lump sum.
- 1231. The new paragraph 1(2) carries forward the existing wording of the current paragraph 1. In conjunction with the increase in the incremental rate to $^{1}/5^{th}$ of 1% for each incremental period provided for in paragraph 2(3) of Schedule 5 (see in relation to section 297(3) above), this sub-paragraph provides a minimum deferral period of five weeks for increments by providing that no increase is payable if the increment would be less than 1%.
- 1232. Paragraph 6 corrects an omission in the current legislation. For the purposes of calculating increments, the intention is that additions to the pension for a dependent husband or wife under sections 83 and 84 of the Contributions and Benefits Act are excluded. As drafted, however, paragraph 2(5)(b) of Schedule 5 only excludes additions under section 83 (paid to a husband for his wife). From April 2010, both sections are replaced by section 83A which equalises the provision of additions for dependent spouses. Paragraph 6(1) therefore substitutes a reference to section 83 with a reference to section 83A; paragraph 6(2) provides that until section 83A comes into effect in 2010, it is to be read as a reference to sections 83 and 84.
- 1233. *Paragraph 7* inserts a new paragraph 2A into Schedule 5 to provide for the calculation of the increase to the weekly pension that will be applicable where a person has elected a lump sum but their deferred pension includes an increase for inheritable GMP increments (see note to paragraph A1(4) above). The increment is to be calculated on that component of the deferred weekly pension alone (the rest being converted to a lump sum).
- 1234. *Paragraph* 8(1) inserts new paragraphs 3A and 3B into Schedule 5.
- 1235. Paragraph 3A provides that a person is entitled to a lump sum if they have both deferred entitlement to their state retirement pension and have elected to receive a lump sum under paragraph A1(1)(b) (or are treated as having made such an election) having deferred their entitlement to their pension for at least 12 months.
- 1236. Paragraph 3B sets out how the lump sum is to be calculated. This is modelled on the same principle as an interest-earning savings account: interest will be applied each week to the amount "saved", and compounded.
- 1237. The weekly amount to which the rate of return will be applied is the amount of pension that the person would have been entitled to had they not deferred (subject to paragraph 3B(5), see below). Retirement pension is payable weekly in advance from the first benefit payday that coincides with, or follows, the date the person is first entitled to the pension. So for example, if a person reaches pensionable age on, say, a Thursday and their pension payday is a Monday, they will not be entitled to any payment for the days preceding that first Monday. At the other end of the claim however, if they cease to be entitled to the pension on for example, a Wednesday, their pension continues in payment to the end of that benefit week.
- 1238. In order to capture accurately the amount of state retirement pension forgone therefore, the definition of "accrual period" will mirror the provisions which determine what constitutes a person's benefit week, and effectively provide that each benefit week

which begins in the deferment period will be a week that counts for the lump sum calculation. This means that days in the period of deferment preceding the first notional payday will be excluded, but days which fall between the end of the deferment period (i.e. the date the pension claim is actually made) and the first date for which weekly pension becomes due will be included.

- 1239. For the purposes of the calculation, the amount of weekly pension forgone includes an invalidity addition³ but excludes increases for a dependent adult or child or any Graduated Retirement Benefit (see below in relation to paragraph 17 of the Schedule). It also includes any increments inherited by the deferrer from a deceased spouse. This corresponds to the definition of "weekly benefit" as used as the basis for the calculation of increments.
- 1240. However, where the deceased spouse has been entitled to increments from deferring their GMP, the increase awarded in respect of those increments (and uprating of those increments) under paragraphs 5 to 6 of Schedule 5 will not form part of the weekly pension forgone for the purpose of the lump sum calculation, but will instead continue to be included as an increase to the weekly pension (cf. note to new paragraph 2A, above).
- 1241. Regulations made under paragraph 3B(5)(b)(iii) will provide for the amount of lump sum to be adjusted to take account of circumstances in which pension would have been reduced or not payable had the person been claiming at the time (for example, if another benefit which overlaps with retirement pension had been in payment, or the person had been serving a prison sentence).
- 1242. The percentage rate that is to apply will be the rate which is 2% higher than the Bank of England base rate, or such higher rate as may be prescribed by affirmative regulations (see *paragraph 19* of the Schedule). The formula at paragraph 3B(3) applies the 52nd root of this figure to the amount accrued in each "accrual period", to provide a compounded rate which at the end of a period of 52 weeks will equal this percentage rate.
- 1243. The following example demonstrates how the formula is intended to be applied. The weekly pension rates and rate of return shown here are to be read as illustrative only.

Assume Miss Smith would have been entitled to retirement pension of £100 per week from April 2005 had she claimed at that point, and that the prescribed interest rate at the start of the period of deferment is 6.00%. This is equivalent to a weekly increase factor of

1.0652 = 1.001121

, where 1.06 refers to a prescribed interest rate of 6.00%.

At the end of the first accrual period, the amount accrued would be:

 $£0.00 + £100.00 \times 1.0652 = £100.11$

(note that in the first week, there is no "accrued amount" to bring forward from the previous week, therefore this is shown as zero).

At the end of the second accrual period the amount accrued would increase to:

£100.11 + £100.00 x 1.0652 = £200.34

At the end of the third accrual period, the amount accrued would increase to:

£200.34 + £100.00 x 1.0652 = £300.67

³ An invalidity addition is an increase added to a person's Category A pension where they were entitled to an age-related addition to their Incapacity Benefit on any day within the eight week period before they reach state pension age. The addition may be extinguished under certain circumstances: paragraph (5) provides that these circumstances are to be ignored for the purposes of the lump sum calculation.

After 52 weeks, Miss Smith would have accrued a lump sum of £5,357.49.

Assume Miss Smith continues to defer and her retirement pension entitlement increases to £103 with effect from April 2006. The lump sum will continue to be calculated in the same manner as above, except that £100 changes to £103. At the end of the first accrual period using the new rate the lump sum would be:

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£5,357.49 + £103.00 x 1.0652 = £5,466.61
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At the end of the second accrual period using the new rate the lump sum would be:

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£5,466.61 + £103.00 x 1.0652 = £5,678.85
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If Miss Smith chose to defer for two years altogether, at the end of March 2007 she would be entitled to a lump sum of £11,197.15.

- 1244. Except where the rate has been set by regulations to give a higher rate than the norm, a change to the Bank of England base rate will automatically trigger a corresponding change in the lump sum rate of return in order to maintain the 2 percentage points differential. It is intended to apply any such new lump sum rate from the start of the first accrual period following a base rate change (paragraph 3B(4)). However, as a contingency, a regulation-making power has been taken to allow for a longer lead-in, in case it proves not to be technically feasible to implement the new rate as quickly as envisaged. Should this arise, these regulations would effectively maintain the legal status of the former rate until the new rate could become operative. This is to avoid the risk of incorrect awards being made in the interval between a new rate being announced and the adjustment being made to the computer systems calculating the lump sum.
- 1245. *Paragraph 8(2)* makes the same provision regarding the exclusion of dependency additions under sections 83 and 84 of the Contributions and Benefits Act before April 2010 for the purposes of calculating the lump sum as made by paragraph 6 above in respect of increments.
- 1246. Paragraph 9 inserts a new paragraph 3C into Schedule 5. This allows the surviving spouse of a deferrer who has died whilst deferring his pension (having deferred for at least 12 months) to be able to choose between "inheriting" increments or a lump sum in respect of his deferment. This choice is only to be exercised when the widow/er is claiming his or her own pension (and has not remarried before reaching state pension age): if the deferrer dies when the spouse is still under state pension age, the amount of increments or lump sum which would have been awarded had the spouse been entitled to his or her pension at the time the deferrer died will be increased annually, broadly to reflect price increases in the period between the deferrer's death and the date the survivor claims his or her pension. (This provision already exists for increments; the equivalent provision for lump sums is made by new paragraph 7B(7) as inserted by paragraph 11 of this Schedule, and by the amendment to section 150 of the Social Security Administration Act 1992, as inserted by paragraphs 20 to22 of this Schedule).
- 1247. Paragraph 3C(3) and (4) make provisions corresponding to those at paragraph A1(2) and (3) deeming the lump sum to be the surviving spouse's choice if no election is made within the prescribed time limit, and enabling the regulations to allow the election to be changed within a "cooling-off" period to be specified in regulations.
- 1248. Paragraph 3C(5) provides that where the deceased was, or would have been, entitled to increments from deferred GMP, the surviving spouse will "inherit" an increase to the weekly pension in respect of that element, regardless of what election is made in relation to the rest of the deceased's deferred entitlement.
- 1249. *Paragraph 10* amends the existing paragraph 4 of Schedule 5 to provide that a surviving spouse who has not remarried before reaching state pension age will be entitled to inherit increments, either where increments were already in payment to the deceased when he died, or where this is the widow/er's preferred option, or where the deceased

had deferred for less than 12 months. The provisions relating to the actual amount of increments the surviving spouse inherits are not amended by this Act and are therefore not described here.

- 1250. *Paragraph 11* inserts new paragraphs 7A and 7B into Schedule 5 which largely replicate paragraphs 3A and 3B in respect of the calculation of the lump sum for a widowed person.
- 1251. The only difference between the two calculations is that the amount of additional pension forgone will be adjusted to reflect the proportion of that pension component which the surviving spouse is entitled to inherit as part of her weekly pension. Paragraph 7B(3) shows the proportion as one-half. This would be modified in respect of additional pension that is derived from SERPS, by the Inherited SERPS regulations⁴, made under section 52(2) of the Welfare Reform and Pensions Act 1999. Paragraph 25 of this Schedule amends section 52(2) so that those regulations may be amended to include references to the lump sum. This will enable the reduction in the inheritable proportion of the additional pension component of the lump sum to be phased in by October 2010, in line with the corresponding changes to inheritable SERPS itself.
- 1252. New paragraph 7C, inserted by *paragraph 12*, provides that the final amount of the lump sum will be rounded to the nearest whole penny. Sub-paragraph (2) provides that when exercising the power to prescribe an interest rate higher than 2% above the Bank of England base rate, the Secretary of State must have regard to the national economic situation and to any other matters which he considers relevant.
- 1253. *Paragraph 14* makes consequential amendments to paragraph 8 of Schedule 5 to include references to the lump sum calculation. In particular, new sub-paragraphs (4) to (6) substitute the existing paragraph 8(4) which prevents increments being inheritable by a surviving spouse in respect of deferred pension that was either wholly or partly based on the survivor's own contributions (i.e. it was either a Category B pension or a Category A pension that was increased by virtue of the spouse's contributory record). This provision is now extended to refer to the calculation of lump sums.
- 1254. *Paragraph 15* inserts a new Schedule 5A into the Contributions and Benefits Act to provide the choice between a lump sum or pension increase where a person has deferred their shared additional pension and how that lump sum or increase is to be calculated.
- 1255. Paragraphs 1, 2, 4 and 5 of the new Schedule 5A largely replicate the provisions made under paragraphs A1, 1, 3A and 3B of the amended Schedule 5 with respect to elections between increments and a lump sum, and the calculation of the lump sum. Paragraph 3 replaces the existing provisions in section 55C of that Act relating to the calculation of increments where shared additional pension is deferred, incorporating the changes to those provisions made under section 50(2) of the Welfare Reform and Pensions Act 1999 to take effect from 2010 and now brought forward.
- 1256. The only significant difference between the lump sum for Category A or B pension and the lump sum for shared additional pension is that, in line with the current provisions on shared additional pension increments, if the person entitled to that pension has subsequently remarried and dies leaving a widow or widower, the surviving partner will not be entitled to inherit the lump sum.
- 1257. *Paragraph 17* amends section 62(1) of the Contributions and Benefits Act so that where entitlement to Graduated Retirement Benefit has been deferred, regulations may provide for the choice between a lump sum or increments for the deferment period.
- 1258. *Paragraph 18* amends section 122(1) of that Act to include a definition of "Bank of England base rate" for the purposes of the lump sum calculation. It also extends the definition of "deferred" and "period of deferment" for the purposes of that Act to cover deferment of shared additional pensions.

⁴ The Social Security (Inherited SERPS) Regulations 2001 (S.I.2001/1085)

- 1259. *Paragraph 19* amends section 176 of that Act to provide that regulations prescribing the percentage rate applicable to the lump sum calculation shall be made by the affirmative procedure.
- 1260. *Paragraphs* 20 to 22 allow a lump sum to be uprated where a surviving spouse has not attained pensionable age when his or her spouse died and is therefore not yet entitled to their own state retirement pension (cf. notes to paragraph 9, above).
- 1261. *Paragraph 24* omits section 50(2) of the Welfare Reform and Pensions Act 1999 which increased the rate at which increments accrue and removed the time limits for accrual in shared additional pension from 2010: these changes are now subsumed within the new Schedule 5A, as enacted by this Schedule.
- 1262. *Paragraph 25* enables the modifications to the Inherited SERPS provisions to be extended to the calculation of the lump sum for surviving spouses (see under paragraph 11, above).
- 1263. *Paragraph 26* restricts a widower from inheriting a lump sum or increments where he attains pensionable age before 6th April 2010 unless he himself was over that age when his wife died. This re-enacts and extends the corresponding provision made by paragraph 21(14) of Schedule 4 to the Pensions Act 1995 which applied in relation to entitlement to increments under the previous version of paragraph 4(1) of Schedule 5 to the Contributions and Benefits Act, and which is now substituted by paragraph 10(2) of this Schedule.
- 1264. *Paragraph* 27 provides a power to make regulations detailing the transitional arrangements that will apply in cases where a period of deferment spans 6 April 2005, the commencement date of these changes.
- 1265. In particular, it is intended that regulations made under this power will provide that any period of deferment that wholly precedes the commencement date will be subject to existing rules. That is, in respect of any such period, only increments at the current rate may be awarded. For the period beginning on the commencement date, the new provisions will apply so that, providing the part of the deferment period starting on the commencement date lasts for at least 12 months, the deferrer will have the choice of a lump sum or increments at the new rate. Corresponding provisions will be made in respect of a surviving spouse's entitlement to inheritable increments or a lump sum.
- 1266. These sections and schedule, which make further provision in respect of deferred retirement pension or deferred shared additional pension and, in particular, introduce the option of a lump sum, involved consideration of Article 1 of Protocol 1 and Article 14 ECHR. Insofar as these Articles may be engaged it is considered that the further provisions for deferral are justifiable.

Miscellaneous

Section 298: Disclosure of state pension information

- 1267. This section amends section 42 of the Child Support, Pensions and Social Security Act 2000 to allow state pension information to be disclosed to agents, third party administrators and others providing certain services to trustees, managers and employers in relation to pension schemes as well as to the trustees, managers or employers themselves. State pension information may be disclosed by the Secretary of State to such persons if the procedures set out in section 42(4)(b) and (5) and the regulations made under them are followed.
- 1268. Section 42(3A) as inserted will more easily allow scheme members to be given a combined pension forecast where advice or forecasts are provided by third parties to the pension scheme managers or trustees rather than being produced by pension scheme managers or trustees themselves. The lack of reference to such third parties in the existing legislation has limited the number of pension schemes able to provide

- combined pension forecasts because it has prevented the supply of state pension information by the Secretary of State. (See also Part 4 of this Act).
- 1269. Subsection (4) inserts a reference in section 42(7) to projections of any lump sum to which a person may be entitled. Subsection (5) amends section 42(11) to include lump sums in the definition of state pension information and to include shared additional pension and graduated retirement benefit in the definition of additional retirement pension.

Section 299: Claims for certain benefits following termination of reciprocal agreement with Australia

- 1270. This section is needed following the termination of the Social Security Agreement between the United Kingdom and Australia with effect from 1st March 2001. The Agreement is set out in Schedule 1 to the Social Security (Australia) Order 1992. The Agreement provided that, where people living permanently in the United Kingdom had previously lived in Australia, their Australian residence counted as periods for which Class 3 National Insurance contributions had been paid for the purpose of determining their entitlement to certain UK benefits. For example, such periods of residence in Australia could help a person to qualify for a basic retirement pension or enhance the rate of basic retirement pension to which they were entitled. The Agreement made reciprocal provision for people living permanently in Australia who had previously lived in the United Kingdom.
- 1271. The Agreement protected the position of those people who were receiving benefits on the basis of the Agreement on 28th February 2001 or who had made a claim for benefits on or before that date on that basis where entitlement began on or before that date (*subsection* (8)). However, the Agreement did not protect the position of those people who had lived in Australia but who had not made a claim for benefits by 1st March 2001, or who had made a claim for benefits before that date but entitlement started on or after that date. The Department for Work and Pensions, with Treasury approval and having notified Parliament, protected the position of these people by paying certain benefits to them on an extra-statutory basis.
- 1272. Upon Royal Assent this section provides that, for the purposes of claims for basic retirement pension, widow's benefits and bereavement benefits made after the termination of the Agreement, certain provisions of the Agreement are treated as continuing in force with modifications. Any week of residence in Australia before 6th April 2001 (and forming part of a period of residence beginning before 1st March 2001) continues to be treated as a week of residence in the United Kingdom during which a voluntary Class 3 National Insurance contribution has been paid. This regularises the statutory basis for the payments which have been made under the extra-statutory scheme (*subsection* (7)).
- 1273. Where reciprocal agreements are modified to take account of changes in UK legislation, there is a power to modify UK legislation as it applies to cases affected by the reciprocal agreements (under the Social Security Administration Act 1992 and the Northern Ireland equivalent). Subsection (4) enables this power to be exercised in relation to the provisions of the Agreement with Australia which are continued in force by this section.