AWFM Fact File

"NEST & other State Pension issues"

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Our other Fact-file "State Pension" gives a guide in particular to the State Second Pension (S2P) and helps to answer the question "Should I contract Out or Contract back in?" This Fact-file aims to deal with more recent developments and in particular the changes being **proposed** both to the State Pension system and to Company pensions. One thing is for sure, the Treasury have a problem which is basically caused by the ageing population and they need to make significant changes to the financial commitment to funding state pensions.

State Pension Proposed Changes

The following is a summary of the main changes proposed in the White Paper published in May 2006:

State Pension Age

The State Pension Age (SPA) will be increased to reflect increases in life expectancy. The female SPA is already scheduled to increase to the male SPA of 65 by 2020. In future, the SPA is likely to rise for both men and women as follows:

- Between 2024 and 2026 to age 66
- Between 2034 and 2036 to age 67
- Between 2044 and 2046 to age 68

Basic State Pension

The link between the Basic State Pension (BSP) and increases in national average earnings (NAE) is to be restored from 2012 ('subject to affordability'). A range of other changes are proposed to the BSP including reducing the number of years needed to qualify for full BSP to 30 years (currently 39 years). This could be beneficial for those who take career breaks, such as for caring responsibilities.

State Second Pension (S2P)

At present, all "Employed" people (unless contracted out – see below) accrue entitlements within S2P, linked to their earnings. This is paid on top of the Basic State Pension. Between 2012 and 2030, S2P may well be downgraded in value, so that by 2030 it provides a lower, flat rate pension.

Contracting Out

At present, individuals or Company pension schemes can choose to contract out, giving up their entitlement to S2P in return for a rebate in their National Insurance contributions which is paid into their personal or occupational pension. From 2012, this *may* no longer be available for those in personal, stakeholder or occupational defined contribution schemes. The Government is planning to consider the future of contracting out within Final Salary schemes too.

Means tested benefits for the low earners

At present the Pension Credit is available for those whose income is below £114.05 per week for a single person (£5,930 p.a.) or £174.05 per week for a couple (£9,050 p.a.). This is reduced where savings are available in excess of £6,000. It is clear that one of the issues the Government face is wanting to encourage people to make their own pension provision whilst protecting the low earners with this minimum income guarantee. At present the really low earners could be better to make no pension or savings provision relying instead on state provision. Any small provision they make can be eaten up by a reduction in state benefits. The planned changes seek to address this problem but as yet we do not see how!

Personal Accounts

The Government is *proposing* a new system of low cost Personal Accounts to encourage people to save for, and take responsibility for, their retirement to be introduced in 2012. This is effectively taking forward the Pensions Commission **National Pensions Savings Scheme (NPSS)** concept. This may be a Government run fund or in may be "out-sourced" to existing pension product providers. The main facets of this proposed scheme are as follows:

Who?
Employees aged 22 or over and earning above £5,000 will be automatically enrolled either into a Personal Account, or if their employer prefers and it meets minimum requirements, into their employer's scheme.

Opt-Outs?
Individuals will be able to opt out, but if they do, they will be auto-enrolled again after three years at which point they can again opt out.

Self-Employed and Unemployed?
The self-employed and those not in paid work may also join. The Government does not believe individuals will need regulated advice before joining – so the Personal Account is being designed as a "no advice" product.

Contributions
Both Companies and their employees will be required to make contributions into the plan. Individuals or Companies may pay in more than the minimum.:

Employees and others
The proposed contribution is 4% of band earnings (which is earnings between £5,000 and £33,000 a year) plus tax relief of 1%.

Employers
Employer's contributions will 3%. The employer contribution will be phased in over three years and there may be support for the smallest businesses, which might receive subsidies or be subject to a longer phasing-in period.

Charges
The Pensions Commission proposed a charge of 0.3% of fund for the NPSS which the industry believes is unrealistically low. The end result will depend on who provides the NPSS scheme.

Investment Based
It is assumed that the new scheme will be investment based using "Life-styling" funds which gradually reduce risk the closer individuals get to retirement. It is unlikely that there will be significant choice or investment funds as there is no facility for advice within these schemes.

Impacts On Other Types Of Scheme
Other pensions such as Personal Pensions should be able to continue in their present format.

What Does This All Mean For You?
We believe that you should plan and prepare for your retirement from an early age. This means making financial provision on a regular basis habitually as soon as you start work. Although for those retiring now, State Pensions provide a good level of basic income, it is rarely enough to live on comfortably. So whether it is paying off debt quicker (as a starter) or making cash savings or paying into pensions or alternative investments, we believe it is essential to make regular provision for your retirement years. Often this may mean looking carefully at what you currently spend your money on now to make sure you are using your money wisely and effectively.

Not many people we come across would be happy to rely on the state's provision entirely, when such low numbers are involved!

If you have any questions or need an independent review of your pension arrangements, please contact us to discuss your situation further. AW Financial Management LLP is an Independent Financial Adviser regulated by the Financial Conduct Authority.

Information given in this document should not be taken as advice as it is intended for guidance only. If you wish to have an assessment of your own situation, you should contact the office for advice.