AWFM Fact File

"State Pensions Explained"

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AW Financial Management LLP

Financial Planning
Independent Financial Advice
Investment & Wealth Management

River House, 1 Maidstone Road, Sidcup, Kent, DA14 5RH
Tel: 01322 669 059   www.awfm.co.uk

There is a very helpful guide to State pensions on the Government website www.direct.gov.uk entitled State pensions – Your guide. This fact-file aims to summarise the answers to some of the more popular questions about State pensions and importantly gives some guidance on the State Pension Reforms being introduced from April 2016. The first part of this fact-file explains the current system. Then we move onto the new system proposed.

3 parts of State Pension
State Pension is made up of:
Basic State Pension
Graduated Retirement Benefit (for employees between 1961 and 1975 only)
Earnings related Pension (was SERPS, now State Second Pension known as S2P)

State Pension age (increases)
Is currently 65 for men and 60 for women born before 6 April 1950. For women born between 6 April 1950 and 6 April 1959 the age increases each year to an eventual retirement age of 65 in line with men. All women born after 6 April 1959 will have 65 as their state retirement age ...until …

From 2024 the state pension age for both men and women will increase for anyone born after 6 April 1959. Again the increase is gradual carried out over a 22 year period in 3 stages. For those now (in 2008) who are aged 50+ the retirement age is still likely to be 65. For those currently in the 40-50 bracket, the state pension age is likely to be about 66. For the 30-40s, it is likely to be 67 and for those below 30 it will be 68.

Expect more changes on this front!

Building up State Pension (Old system)
Entitlement is built up by paying National Insurance (NI) contributions eligible to be classed as a Qualifying payment. For women born after 6 April 1950 and men born after 6 April 1945 you will need 30 qualifying years (reduced from 44 & 39). Each qualifying year will generate 1/30th of the full basic pension.

> Employees gain a year's credit if their earnings are above £110 per week (2009/10). This is known as the Primary Threshold. If you earn less than £110 but more than £95 per week you are treated as if you had paid NI and therefore credited with a qualifying year.
> Self-employed people must pay £2.40 per week (2009/10) as a flat rate to earn a qualifying year.
> If you are not working, you can still build up state pension credits if you are ill, unemployed and registered as looking for work.

Home Responsibilities Protection is being replaced for those reaching state pension age after 2010. Existing benefits under HRP will be converted to the new system.

Improving your State Pension
There are a few ways in which you can make an improvement to your state pension entitlement:
Use your husband/wife/civil partners NI record – Up to 60% of the basic state pension is available this way if you cannot generate enough credit yourself.

Buying additional years - Available for those who have missed qualifying years. Contributions normally have to be made within 6 years of the end of the relevant year you have missed. ie for 2007/08 you need to settle by 2013/4.

How much – Basic State Pension?

Single person in 2009/10	£95.25 per week
Married couple in 2009/10	£152.30 per week (for those where only one partner qualifies in their own right)

How much – Earnings Related Pension (SERPS/S2P)?
It is not possible to say how much additional pension might be payable for you. You therefore need to obtain a State Pension forecast to make a reasonable assessment. This is crucial to your retirement planning. The calculation of S2P benefits is complicated and quite frankly is highly likely to be changed in my opinion, but at the present time is (based on 2009/10 values):

40% of earnings falling between £4,940 & £13,900 (max £3,584 pa)
10% of earnings falling between £13,900 & £31,800 (max £1,790 pa)
20% of earnings falling between £31,800 & £40,040 (max £1,648 pa)

In today's terms therefore the maximum additional State Pension could equate to around £7,022 pa.

State Pension increases
The Government decides on the rate of increase applicable to State Pensions each year. This makes planning difficult.

Pension Credit
If you are over 60 and Pension Credit will guarantee that you have a minimum income (2009/10 tax year) of:

£130 per week if you are single (£6,760 per annum)
£198 per week if you have a partner (£10,296 per annum)

Between 6 April 2010 and 5 April 2020 the qualifying age for Pension Credit will rise to be in line with the State Pension age for all.

What happens on death?
This is not at all straightforward either. Firstly Basic State Pension – it is likely that the basic state pension will be reduced to your own single person's full allowance. With the earnings related pension, it is likely that the income paid to your partner will continue to be paid to you at a reduced rate.

Deferring State Pension
It is possible to defer your State Pension once you reach State Pension age. You will then have two options (which you decide on when you draw your benefits):

- Extra income - You build up 1% extra State Pension for every 5 weeks you defer your pension. This works out to be about a 10.4% increase for one full year's deferment.
- Lump sum – You could receive the back-payments that were due to you from your normal State Pension age, with interest added at 2% above the Bank of England's base rate. The lump sum is taxable.

Changes Effective for People Retiring after April 2016
A flat-rated pension of £144 per week (in today's terms) will been introduced for those people retiring after April 2016. Eventually, this will replace the current complicated system set out above. For those who have been part of the old system and the new system, there will be an amalgamated benefit payable which for the time being will also be quite difficult to calculate.

In order for a younger person to benefit fully from the new State Pension they will need to have contributed to through NI contributions to the scheme for 35 years (note this is 5 years more than under the present system). Contribution terms of less than 35 years will produce a proportional pension – 20 years would give 20/35s of the full amount.

The State Pension age will be 67 for those retiring after 2028.

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.

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