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NPC submission to the Independent Public Service Pensions Commission

1. Introduction

1.1 The National Pensioners Convention (NPC) is Britain's largest pensioner organisation representing around 1.5m older people, active in over 1000 affiliated groups. The NPC is run by and for pensioners and campaigns for improvements to their income, health and welfare.

2. Background

2.1 At present, Second Tier State Pensions (SERPS, Graduated Pensions and S2P) and public sector pensions are uprated each April based on inflation as recorded in the previous September.

2.2 Since 1972, the measure of inflation has been the Retail Price Index (RPI) and both existing pensioners and employees have been led to believe by both pension scheme literature and official pronouncements that the RPI link would be maintained. As a result, many have made financial choices based on that understanding.

2.3 However, in the Emergency Budget on 22 June 2010, the Chancellor announced that in future the inflationary measure will be that of the generally lower, Consumer Price Index (CPI). Since that time, it has also emerged that the CPI will be used as the inflation measure for the basic state pension after 2011, and in up to 60% of defined benefit/final salary private pension schemes that do not specify RPI in their rules.

2.4 The change from RPI to CPI clearly therefore affects both existing pensioners through their first and second state and occupational pensions, as well as existing workers through their public or private occupational pensions, and raises very serious concerns about the long-term value of those schemes.

3. Pre-election assurances

3.1 Prior to the election, there was considerable speculation in the media about the future of public sector pensions. One of our affiliates; the Civil Service Pensioners' Alliance sought assurances from the three main political parties as to the question of index-linking and accrued rights.

3.2 At a meeting held on 30 March 2010, Angela Eagle said on behalf of the Labour Party *"Following the agreement for change reached with the unions in*

2007, we are satisfied that public sector pensions are affordable, sustainable and fair. We have no plans to change the current index-linking arrangements.”

3.3 In a letter dated 27 April 2010, Philip Hammond the then Shadow Chief Secretary to the Treasury said: *“Indexation of pensions in payment is an established part of pensions legislation. The Conservative Party has no plans to change the current index-linking of public sector pensions in payment. We agree with the view that the right to indexation of pensions already accrued is part of the accrued pension rights and those rights will be protected.”*

3.4 The then Liberal Democrat Shadow Pensions Minister, and now Pensions Minister, Steve Webb MP also said in a letter dated 12 April 2010: *“We are very clear that all accrued rights should be honoured: a pension promise made should be a pension promise kept. Therefore we would not make any changes to pension rights that have already been built up. I have confirmed that I regard accrued index-linked rights as protected.”*

3.5 Furthermore, at a conference held by the Public Service Pensioners’ Council in April 2010, all three pensions spokespersons stressed that any changes to public sector pensions would have a long lead-in time and would be subject to full consultation.

3.6 However, despite such reassurances, the Coalition government has now announced that it intends to change the indexation of basic and second state pensions, alongside public and private occupational pensions, without any consultation. This is of particular concern given that such a move was not outlined in either of the Coalition parties’ election manifestos. Even more surprising is that the government has made such an announcement almost a year before your Commission is due to report its findings.

4. The difference between RPI and CPI

4.1 In general terms, the CPI is usually less favourable than the RPI, and had pensions been linked to the CPI for the past 10 years, they would now be worth around 12% less than their current value.

4.2 Whilst the Budget did not forecast CPI inflation in September, it did include both RPI and CPI forecasts for Q4 of each year. The tables below therefore assume that the difference between CPI inflation and RPI inflation in September is the same as in Q4. For example, the Budget projects that RPI inflation will be 4.2% in September 2010, that RPI inflation will be 3.7% in Q4 2010 and that CPI inflation will be 2.7% in Q4 2010. Based on this 1% gap, we have assumed CPI inflation will be 3.2% in September 2010. The table shows inflation in each month on this basis:

	2010	2011	2012	2013	2014	2015
RPI (Sept)	4.2%	3.4%	3.0%	3.2%	3.4%	3.5%
CPI (Sept)	3.2%	2.6%	1.7%	1.9%	2.0%	2.0%

4.3 The second table shows how this would affect a pension of £10,000 before pension increases are rounded:

	No w	April 2011	April 2012	April 2013	April 2014	April 2015	April 2016
RPI uprating	10, 000	10,42 0	10,77 4	11,09 8	11,45 3	11,84 2	12,25 6
CPI uprating	10, 000	10,32 0	10,58 8	10,76 8	10,97 3	11,19 2	11,41 6

4.4 Assuming that increases in inflation remain, at least for the next few years, higher than average earnings, the impact that using CPI instead of RPI would have on a single basic state pension is as follows:

	N o w	April 2011	April 2012	April 2013	April 2014	April 2015	April 2016
RPI uprating	97 .6 5	101.7 5	105.2 0	108.3 5	111.8 0	115.6 0	119.6 5
CPI uprating	97 .6 5	100.7 5	103.3 5	105.1 0	107.1 0	109.2 5	111.4 5
2.5% uprating	97 .6 5	100.1 0	102.6 0	105.1 5	107.7 5	110.4 5	113.2 0

5. A contradiction of policy

5.1 The announced change in indexation also appears to have highlighted a dichotomy in government policy. Paragraph 1.106 of the Budget Report says *“The CPI provides a more appropriate measure of benefit and pension recipients’ inflation experiences than RPI, because it excludes the majority of housing costs faced by homeowners (low income households are subsidised separately through Housing Benefit, and the majority of pensioners own their home outright), and differences in calculation mean it may be considered a better representation of the way consumers change their consumption patterns in response to price changes. This will also ensure consistency with the measure of inflation used by the Bank of England.”*

5.2 However, paragraph 1 of the Coalition Agreement “Our Programme for Government” says *“We will work with the Bank of England to investigate how the process of including housing costs in the CPI measure of inflation can be accelerated.”*

5.3 We do not accept that CPI is a more appropriate measure for pensioners, because the vast majority are still liable for Council Tax and pay for the upkeep and repair of their property. As they grow older they are less able to undertake these tasks themselves, so must pay others to do the work for them and do so from an increasingly limited income. In addition, an increasing number of pensioners still have a mortgage, and this is likely to increase for future generations of retirees who now start buying property at a later stage in their lives. All of these costs are excluded from CPI, which, in any event, is not truly representative of pensioner expenditure. The proposed move from RPI to CPI for both state and public service pensions is a cynical attempt by government to save expenditure, at the expense of those least able to afford it.

6. The public versus private pension debate

6.1 Over the last year or so, there has been much criticism in the media of public service pensions, led largely by the representatives of those employers who have shamelessly withdrawn from pension provision for their own employees. However, the debate is generally rather selective in its approach.

6.2 The reality is that public service employees have paid for their pensions either by way of actual contributions or by way of salary sacrifice. Moreover, it is completely false to argue that somehow the general public pay for public sector pensions, but don't pay for those in the private sector. Any private company will include in the price of its products or services a proportion of income that will go towards paying the wages and other benefits of its employees, such as pensions. In this way, tax payers and consumers are making a contribution to the pension funds of almost all those workers that have some kind of occupational pension – regardless of whether it is in the public or private sector.

6.3 The UK's pensions policy is at a crossroads. The reliance on a combination of means-tested support for existing pensioners and decent occupational pensions for future generations is being seriously undermined by an unsustainable policy and the weakness of the private pensions system. What lies at the heart of the approach by successive governments to pensions is a simple contradiction. The pension strategy since 1997, including the reforms in the 2007 Pension Act, have not only failed to tackle existing pensioner poverty – they may also be making it worse for future generations of pensioners as well.

6.4 The current state pension is one of the least adequate in Europe, and for decades UK governments of all complexions have justified that by reference to previously good occupational pension provision. That provision is now unravelling.

6.5 An estimated 5m workers are currently paying into defined contribution/money purchase schemes. These defined contribution pensions invest in a mix of shares, property, cash and bonds, but more than 90% of people opt for the default fund, where between 75 to 100% of investment is in shares. With share values plunging, a £100,000 pension pot which would

previously have bought a monthly income of £620, will now buy just £490. For the average worker, their pension pot is more likely to be around £25,000 and their monthly income closer to £160.

6.6 For those with a defined benefit/final salary scheme, the picture is very similar. Most commentators have already begun saying goodbye to the final salary scheme, with the National Association of Pensions Funds reporting that 87% of final salary schemes have closed to new entrants including high street names such as Boots, Barclays, Morrisons, Royal Bank of Scotland, the Post Office, IBM and Rentokil. 18% are also closed to existing staff – and this is likely to rise to 39% in the coming year.

6.7 These developments therefore strengthen the case for a decent state first and second pension system that can provide real financial security for all in retirement. Unless the government grasps the challenges on pensions they face, future generations of pensioners will be condemned to a late life of means-tested state benefits and/or poverty.

7. Recommendations

7.1 The Commission should recommend the government honour the long-term commitment to RPI indexation for state, public and private sector pension provision and introduce a quadruple guarantee of increases in line with earnings, RPI, CPI or 2.5%, whichever is highest.

7.2 The Commission should recommend the government produce a short to medium-term plan showing how the basic state pension for all older people can be raised to the official poverty level.

7.3 The Commission should undertake further research into the extent of public and private sector pension provision and produce information that would give a more accurate picture to the general public of the costs involved.