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**Pension Reform in the UK: re-casting the public/private mix in pension provision
1997-2000**

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Introduction

"The UK is one of the few countries in Europe that is not facing a serious pension crisis. The reasons for this are straight forward: state pensions (both in terms of replacement ratio and as a proportion of average earnings) are among the lowest in Europe, the UK has a long-standing funded private pension sector ... and its governments have, since the beginning of the 1980s, taken measures to prevent a pension crisis developing. These measures have involved making systematic cuts in unfunded state pension provisions and increasingly transferring the burden of providing pensions to the funded private sector, principally on a defined contribution basis". (Blake, 1997, p223.)

The growing reliance on private pension is confronting policy makers with a new range of problems. The increase in private provision may have reduced some of the obligations on the state. However, it raises the issue of whether private pension providers will be able to deliver a high quality of provision for future pensioners. A highly privatised constellation of pension arrangements forces politicians to consider the issue of regulation, and the dilemmas posed in trying to balance risk and regulation. Until the 1980s, the risks associated with private pensions had not given rise to public scandals. The historical section of this paper shows how the state attempted to regulate private pensions by stipulating quality requirements in return for permission to 'contract-out' of the state scheme. However, two major disasters led to a re-consideration of the regulatory regime in the UK. The first was the Maxwell scandal in 1992, in which the late Robert Maxwell, proprietor of Mirror Group newspapers, used the company pension scheme to support his ailing business empire (Blake, 1995). This case led to the establishment of a public inquiry and one of the first

major reports on the future of regulation. The second scandal involved the mis-selling of Personal Pensions in December 1993. It emerged that, from 1988, 500,000 members of occupational pension schemes had switched to Personal Pensions as a result of bad advice from those marketing the product (Blake, 1997, p227). A range of public sector employees left good occupational pension schemes, which offered index-linked pensions based on final salary. They were persuaded to move to Personal Pensions, which took twenty five per cent of the transfer value in commissions and administrative charges. In addition, the employer did not contribute. These scandals increased public awareness of the degree of risk associated with market provision and a re-evaluation of the regulatory regime. However, there is a fundamental problem in attempting to regulate a voluntary activity. In addition, in a climate in which both political parties wish to increase private sector provision, increasing regulation will act as a disincentive on the private sector. Moreover, the reduction of state provision means that consumers are not in a position to exercise choice. In this sense, UK governments have created a situation in which they are highly dependent on the private sector.

Although the reform of regulation was initially a reaction to high profile scandals, more recently, it has been influenced by the uncertainties that have emerged in recent years. The history of privatisation in the UK has shown that government does not necessarily avoid blame when things go wrong with a privatised service. As a result, the current problems in the private pension sector, such as the trend away from final salary schemes, are likely to keep the regulation issue at the forefront of political debate.

The Regulation of Occupational Pensions 1959-1997

The most potent form of regulation that has been employed in relationship to the private sector has been the conditions under which private occupational schemes have been allowed to “contract-out” of the state pension scheme. In general terms, the Occupational Pensions Board operating out of the Department of Social Security has implemented this form of regulation. The contracting-out conditions set standards for the quality of occupational schemes. They referred to how pensions would be protected against inflation once they were in payment and to the preservation of pension rights when employees moved from one

job to another. The standards imposed by government regulation had a profound impact on the growth of occupational pension schemes. As the next section shows, weak standards of regulation, combined with an inadequate state provision, led to a climate in which the number of occupational schemes increased and became well established. When nearly half the work force became members of occupational schemes, the role of the state as a regulator changed. There were high political costs involved in imposing forms of regulation that would be inimical to the private sector. The extent of its coverage had created an important interest group, and generated a high level of political risks for government wishing to increase state regulation.

In 1979, when the Thatcher administration was elected, approximately half the British work force was covered by private occupational schemes. Occupational pensions had experienced a period of growth after the Second World War. In 1936 they covered thirteen percent of the work force and by 1956 this increased to thirty three percent (Hannah, 1986: 67). The real growth in private sector provision began in the 1950s in response to the deficiencies of the Beveridge system of National Insurance. Financed by flat-rate contributions that delivered flat-rate benefits, the system faced two intractable problems. First of all, by the 1950s it was clear it had failed to protect pensioners from poverty and during this decade the numbers forced to claim means-tested National Assistance rose. Since a central objective of the Beveridge plan was to eliminate means-testing, this was politically unacceptable to many. Secondly, the flat-rate method of financing pensions was incompatible with the need to increase the level of the basic state pension. Contributions had to be determined by what the poorest members of the work-force could be reasonably expected to pay. Thus both the Labour and Conservative parties were seeking alternative solutions. The Labour Party sought to extend state provision whereas the Conservatives looked to the private sector.

The Conservative Strategy 1958-79: Encouraging the private sector

A key feature of Conservative Party policy throughout the post-war era has been the commitment to market provision. The retrenchment of state superannuation in the 1980s was completely in keeping with past conservative policy which was to ensure that the state

provision remained modest in order to encourage private provision. In late 1950s, the Conservative agenda was determined by the problems of financing the basic state pension and the need to respond to the Labour Party's proposals for a state superannuation scheme. 1958 was an important date because the pension legislation of 1946 had stipulated that those reaching retirement without a complete contributions record would be "blanketed-in" and would become eligible for a full state pension. Thus the idea of instituting earnings-related contributions was attractive because it was a method of increasing revenue to finance increased expenditure. While policy-makers in Sweden and Germany were concentrating on the development of state superannuation, the British Conservatives were steadfast in their support for market solutions. The 1959 National Insurance Act instituted a graduated pension scheme which was largely used to finance the basic state pension rather than provide earnings-related benefits (Hecló, 1974). The Boyd-Carpenter scheme, as it was known, levied earnings-related contributions on all those earning between £9 and £15 per week at a time when average male earnings were about £13 a week. Thus the higher paid were exempt and the lower paid were not eligible to join the scheme and would be dependent on the basic state pension. Moreover, the graduated benefits it would provide were very poor value for the contributions paid and were not protected against inflation. However, the legislation is very important in its use of the device of contracting out. Occupational pension schemes were allowed to contract-out on relatively easy terms. As Hecló comments:

"The Conservative government's new pension plan, which came into effect in April 1961, not only avoided hindering the development of occupational schemes but provided a positive fillip to the entire private sector...By April 1961 the number of contracted-out employees was 4.1 million rather than the 2.5 million originally estimated by the government"(Hecló, 1974: 273).

The Conservative government established a strategy which would be pursued by subsequent Conservative administrations of facilitating private sector growth by relaxed regulatory conditions and restricting the quality of state provision. As Hannah writes:

"As the insurance world recognised, Boyd-Carpenter's pension plan was 'a political gimmick, not a pension scheme'. None the less, as it left them a relatively clear field, the main pension interests understandably supported it...The Conservative strategy had been to achieve as little for the state scheme as politically possible; and, if the primary measure of success is the consonance of objectives and achievements, their graduated scheme must rank as the most successful piece of pension legislation ever. The plan achieved little in the way of earnings-related state pension and it did so at considerable cost" (Hannah, 1986:58)

The result was a substantial growth in the size of the occupational sector. At the time of the Boyd Carpenter scheme, one third of the work force had been covered and this increased to nearly half during the 1960s.

Table 1: Work force covered by occupational pension schemes

1956	8 million
1963	11.1 million
1967	12.2 million

The policy of contracting-out transformed the insurance industry into a powerful interest group. However, it is important to recognise that a contracting-out mechanism is not the sole factor in determining the numbers who will take advantage of such a facility. Two other factors are involved in the equation. First of all, the terms of the contracting out conditions can either reduce or increase the eligibility of private schemes. Secondly, the quality of public provision will influence the numbers who wish to select private provision - a high standard of public provision will limit the numbers contracting out.

The Conservative Party continued to encourage the private sector when it returned to office in 1970 although they still accepted a limited role for the state. Heclo argues that the insurance industry itself opposed the idea of complete private insurance because they feared that this would eventually lead to state regulation and would limit the high level of freedom from state interference the industry had enjoyed hitherto. As Hannah suggests, many in the pensions industry were concerned at the loss of the 1969 Crossman scheme which would

have introduced state superannuation, and were anxious to achieve some type of stability. Indeed, many sections of the pensions industry were concerned by the more radical elements within the Conservative Party:

The Labour Party strategy: state superannuation and partnership with the private sector

The development of National Superannuation: Labour's Plan for Security in Old Age in 1957 represented an attempt to reconstruct the Beveridge scheme, launch a major state superannuation plan, and regulate private sector provision. The Labour party sought to both increase the level of income maintenance for the elderly and to move the financing of state pensions onto a sound financial footing by instituting a system of earnings-related contributions and benefits. The scheme was developed by the Labour Party spokesman, Richard Crossman in conjunction with Professor Richard Titmuss and Brian Abel-Smith of the London School of Economics, and represented a radical innovation in pension policy, promising (according to the slogan of the time) to deliver "Half Pay on Retirement" (Labour Party: 1957). The Beveridge pension scheme was replacing eighteen percent of average male earnings and the hope was to increase this to fifty percent of the final salary based on average earnings. Thereafter, the pension would be inflation-proofed so that it would maintain its value. The scheme would not pay out benefits in strict proportion to contributions but contain a redistributive formula which would allow poorer pensioners to benefit from a better pension than their contribution record allowed. This was to be financed by more affluent workers who would in turn receive a less generous pension than their contributions dictated. The scheme also had short-term political attractions in that it would enable the Government to fund a fifty percent increase in the existing Beveridge flat-rate pension and would thus solve the problem of poverty among existing pensioners - this too would be protected against inflation. The scheme was partly inspired by private sector occupational provision and, in their advocacy of the new proposals, Labour Party policy makers made much of the gulf between the financial condition of private sector pensioners and those dependent on state support. Occupational pensions were providing a retirement income of between a half and two-thirds of final salary. However, the Labour Party's

policy-makers were highly critical of the private sector because industrial workers rarely had access to occupational schemes. In addition, they were regarded as a flawed system of provision because a change in employment usually meant the employee forfeited their contributions and had to start again with a new firm. Moreover, they deprecated the unfairness of giving substantial tax concessions to occupational schemes that would only benefit a minority of the work-force. A new state scheme would necessitate some regulation of the relationship between the state and the private sector. Would it be compulsory for all workers to join the state scheme and thus pay twice for pension provision if they had an occupational pension, or would private sector schemes be allowed to contract-out? The Labour Party envisaged some contracting-out but only if the insurance companies could meet some extremely stringent conditions. Benefits and contributions would have to compare favourably with those offered by the state and there would have to be complete transferability of pension rights from one place of employment to another. There is no doubt that the private sector would have found it extremely difficult to meet these conditions - particularly the provision of inflation-proofed pensions and thus very few firms would have met the contracting-out requirements:

"Occupational pensions by now already covered a third or more of work-force, and many employers were considering introducing, upgrading or expanding schemes. This did, then, probably represent the last practical moment at which a state earnings-related pension scheme could have wiped out the bulk of demand for private provision in Britain. When the Labour scheme was announced, the shares of insurance companies fell sharply. Shareholders were right to be worried: this scheme could kill the bulk of their expanding business in pensions." (Hannah, 1986: 56)

Although National Superannuation remained the basis for Labour pension reforms when it came to office in 1964, the growth in private sector provision led to a change of policy. The Labour Party moved from guarded hostility towards private provision to an advocacy of accommodation and partnership. Although they were clearly differentiated from the Conservatives by their belief in a large state earnings related scheme, the price they were prepared to pay was the acceptance of the role of the private sector and a continuation of

preferential treatment towards it. If we look at the general trend in party policy, the somewhat aggressive attitude towards the private sector exhibited in the 1950s was something of an aberration. In fact, between 1959-1964 when the Party continued to refine its plans the issue of regulating the private sector was hardly discussed.

The most notable contrast between the 1957 proposals and the 1969 White Paper lay in the proposals for contracting-out. Labour's National Superannuation allowed private occupational schemes to contract-out of the state scheme provided that they could match the benefits offered by the state scheme (Cmnd. 3883, 1969). As Tony Lynes noted, the better the state scheme the less contracting-out there would be. The Conservative Graduated scheme of 1961 had deliberately provided modest benefits so that occupational schemes would be able to offer equivalent benefits and thus be able to contract-out. National Superannuation deliberately set out to provide benefits that occupational schemes had shown themselves incapable of delivering: guaranteed inflation-proof pensions on retirement, with the possibility of increases in real value after retirement; a pension formula giving better value to the lower paid; and payment of full earnings-related pension after 40 years. Thus it was never clear how any occupational scheme would be able to measure up to the standard of National Superannuation. However, the 1969 proposals offered "partial contracting-out", a device which was:

"Assiduously promoted by the some of the brighter elements of the insurance industry, who saw it as a way of preserving their freedom to sell the traditional non-dynamic type of pension scheme regardless of any improvements in the State scheme. Its adoption in the White Paper represents a major political victory for the life officers". (Lynes, 1969)

Partial contracting-out was indeed a major concession to the insurance industry. Instead of providing comparable benefits to the state scheme, occupational schemes would merely have to offer pensions of a fixed cash value, with no requirement that they should be protected against inflation or geared to the rising living standards of the community, either during the individual's working life or after his/her retirement. Nor would there be any weighting in favour of the lower paid, and maximum benefits would be paid only to those

who contributed for the whole of their working lives. The schemes which contracted-out would not have to meet the generous widows' benefits offered by the state scheme. However, the White Paper proposed that the state should protect those who contributed to the contracted-out schemes. The state would undertake to pay the whole pension, calculated as if the individual had not contracted-out, minus the amount due from the occupational scheme. Thus, the cost of pension increases would be met by the State, the occupational scheme merely being required to continue paying a fixed amount of pension regardless of changes in the value of money or the general level of earnings. Similarly, the state was to pay the whole of the widows' pension. Moreover, the employers and employees who participated in schemes that contracted-out of the state scheme would pay a reduced (or "abated") contribution to the state scheme. In addition, the ceiling placed on contributions would protect the interests of the private sector. This was seen as an attempt to accommodate the private sector by leaving them free to cover higher paid employees who would not be eligible for the state scheme.

There were three principal objections to the concept of partial contracting-out. In the first place, critics of private pensions felt that the occupational schemes provided an inadequate service. Secondly, it was seen as objectionable that the state should subsidise private schemes by providing the types of benefits that they found impossible to deliver. Lastly, it was argued that from the political and social stand-point, Crossman had given way to the insurance industry and accepted the role of the private sector, and they would continue to invest their surpluses where and how they chose. However, the Labour party was defeated in the 1970 general election and the Crossman scheme failed to reach the statute book. The failure to establish a state superannuation scheme in the 1960s injected an important period of delay that, in essence, perpetuated the trajectory established after the war.

The Labour party in the 1970s (DHSS 1974) eventually launched a second tier of earnings-related provision. The scheme proposed an accommodation based on partnership between the two sectors and one in which the private sector would be allowed to compete with the state on more than equal terms. There are two principle explanations for this outcome: firstly, the functional growth of the private pension industry constrained the options available

to the government; and secondly, the absence of any political will or ideological imperative within the Labour party itself dictating that the Party should restrict the private sector. The circumstances of 1974-5 were hardly congenial. Labour's small majority in parliament, the imminence of a second election and the need to implement legislation as expeditiously as possible did not encourage a bold challenge to the private sector. Moreover, the memory of the complex, and at times acrimonious negotiations in 1969 over contracting-out was a disincentive to raising the issue. However, irrespective of the circumstances in which the Labour government found itself, it is important to emphasise that the Party's stance towards the private sector had been vague and ambivalent since 1959 and it was implicitly assumed that private pensions would co-exist with the state sector. In fact the majority of the Party were more concerned with the position of existing pensioners and increasing the basic flat rate pension whilst trade unions with an interest in occupational pensions, in particular public sector unions, clearly wanted provision for contracting out.

The terms on which the Labour Government allowed occupational pension to contract-out of the state scheme were generous because they were based on a form of subsidised competition. The most important element of this was the Government's commitment to underwrite the inflation-proofing of occupational pensions. Private schemes did not provide any indexation for the pension once it was in payment. Therefore, the Government undertook to subsidise the private sector by stipulating that occupational schemes must provide a guaranteed minimum pension at the point of retirement. Thereafter, the Government undertook to provide inflation-proofing for pensioners in occupational schemes. These terms proved highly satisfactory and in 1979 there were 11.6 million occupational pension scheme members, while only 1.3 million choose to contract-in.

In order to understand the arrangements the Conservative inherited in 1979 it is necessary to examine the Labour party's development of a two-tier system of provision. The second tier of pension provision should be viewed in conjunction with the 29 percent increase in the basic state pension made in 1974. The basic pension was to be reviewed on an annual basis and would be indexed in line with either rises in national average earnings or prices, whichever was the higher. The SERPS pension was based on a formula that paid benefits

equivalent to twenty five percent of the best twenty years of lifetime earnings and was indexed in line with inflation. The aim was to replace twenty-five percent of average earnings between the base level and the earnings ceiling. The base level corresponded to the level of the basic state pension and the ceiling was set at seven times that amount. The scheme began in 1978 and had a twenty-year build up period so that a full earnings related second tier would be available in 1998.

The Conservative retrenchment strategy 1979-97

The shape of the British welfare state at the point at which the Conservatives came to power in 1979 is critical to understanding the strategy of retrenchment that was adopted, and the relative ease with which it was implemented. The difficulties and delays in launching any type of state superannuation policy meant that the State Earnings Related Superannuation scheme was only recently established, and not paying out full benefits. By contrast, occupational schemes had been growing in strength. Some authors have suggested that the impact of the Conservative's retrenchment strategy is often over-estimated (Pierson, 1996). In fact, past policy allowed the Conservatives to pursue a course of gradual residualisation which had important consequences for the shape of welfare provision. Equally, the legacy of past policy meant that there was an absence of well-established and powerful interests in defence of the state sector. The strength of the private sector and the corresponding weakness of the state sector meant that the Conservatives did not face 'veto points' or interest groups which would obstruct their agenda. Ironically, the major interest group that blocked certain policy proposals was the insurance industry itself.

The Conservative strategy was characterised by their determination to alter the balance of power between the public and the private sector decisively. However, this did not necessarily mean all out privatisation. A range of measures gradually residualised the state sector and correspondingly encouraged the growth of the private sector. In 1980, the Conservatives abolished the indexation mechanism which linked the basic state pension to increases in national average earnings. The impact of this measure has often been overlooked. It meant that the basic element of the state pension would progressive decline in

value. In 1979 it represented around 20 percent of average male earnings. This proportion was predicted to decline to around 9 percent by 2020.

The Government's strategy was heavily influenced by their objectives in economic policy, in particular the drive to reduce public expenditure as an essential pre-condition for reducing levels of personal taxation which the Chancellor of the Exchequer, Nigel Lawson linked to his strategy for economic growth. This necessarily implied that the levels of social expenditure would be scrutinised.

In 1985, the Secretary of State, Norman Fowler launched his review of social security, the centre piece of which was the abolition of SERPS. His vision was to substitute state earnings related insurance with a system of private insurance. The state would continue to provide the first tier of pension provision, but thereafter, all pension provision would be provided by the private sector. Since SERPS covered all those not already in private occupational schemes this would affect some nine million people (approximately half of all those in employment), and represented a substantial shift in the public/private mix of provision. The basic state pension, although universal in coverage, would become a diminishing component of the post retirement income. The key point is that even to contemplate such a move, the Conservatives needed a large and advanced private pension industry. In contrast to other areas, such as private health insurance, the industry was already well established.

At the ideological level, the privatisation of SERPS was an attractive option. However, in political terms, the abolition of SERPS was less attractive because the scheme had only been in operation since 1978 and thus any savings on the cost of provision would not be visible until the turn of the century and beyond. This was at odds with the Chancellor's immediate requirements for early reductions in public expenditure to facilitate cuts in personal taxation.

Ironically, the Government's proposal to abolish SERPS in its entirety did not meet with an enthusiastic reception from its own supporters. The National Association of Pension Funds

(the private pension organisation) and the major life assurance companies opposed the proposal (Atkinson, 1991: 9), as did the employers organisation, the C.B.I. and the Government's own pensions advisers (Deakin, 1994: 132). The strength of this resistance from the Government's own natural supporters reflected the inflexibility of the private market and their reluctance to become involved with the less profitable sectors of the pensions business. The result was the Government's White Paper of December 1985 proposed to scale down SERPS in line with Nigel Lawson's preferences and Norman Fowler's regret (Deakin, *ibid.* 134-5).

The 1986 Social Security Act extended privatisation and reduced the value of the State Earnings Related Pension. The amendments to SERPS made it less generous for anyone retiring after 1999. Instead of being based on a replacement value of twenty-five percent of the best twenty years of earnings, the formula was revised so that the pensioner would only receive twenty percent of earnings. Furthermore this would be calculated over the lifetime average rather than the best twenty years. In addition, a widow would only receive half her husband's pension rights. The poorer benefits obviously made the private sector more attractive. However, the question arises of how the Government was able to make these changes without attracting further criticism given the high level of public sympathy for pensioners. SERPS was almost unknown as the Green Paper showed and had only recently come into operation. Moreover, all those in contracted-out schemes were not affected. Thus, the proposals affected the poorest pensioners and it is not clear that their full implications were recognised.

Aside from reducing the value of the state pensions, the Government took more active steps to encourage the private pension market. The Government made the requirements imposed on occupational schemes more lenient. They allowed "money purchase" schemes (defined contribution) to contract out. These schemes set a minimum contribution but do not guarantee what the pension will be on the date of retirement (Atkinson, 1991: 10). This move enabled more occupational schemes to contract-out and was accompanied by the introduction of personal pensions.

In July 1988, Personal Pensions were launched, giving the contributor the choice of whether to replace their occupational pension or SERPS with a personal pension. The scheme attracted a great deal of attention and was extensively advertised by the financial services industry. Personal pensions were another area where the Government weighted the dice in favour of private provision. Contributors were encouraged to opt for a personal pension with considerable financial inducements. Those electing to opt out of SERPS were able to use the contributions they would have paid in to the state scheme to buy a personal pension and would also receive a further two- percent from the Exchequer to add to their contribution. This subsidy would be paid on an annual basis until 1993. Thereafter, the subsidy continued at a reduced rate. Needless to say, this was a useful selling point in that it created the over-heated atmosphere of a limited special offer. Five million people bought personal pensions further shifting the public/private balance in favour of the private sector.

Table 2: Employees in Pensions Schemes

Source: Davis (1993)

Total in SERPS	7.9m
Total contracted out	13.8m
Total employed work-force	21.7m

However, by the 1990s, private sector expansion seemed to have reached a natural ceiling. Further growth in the personal pension sector was constrained by a number of factors. First of all, they are expensive because they are sold as individual contracts between the insurance company and the employee and are subject to high administration and transaction costs. Secondly, only a relatively small number of the work-force that were not already in an occupational scheme would be suitable for a personal pension. A substantial proportion of middle to high wage earners was already in occupational schemes. Only thirty four percent of those in employment not already covered by an occupational pension earned more than £10,000 p.a., indeed. forty four percent earn less than £6,000 p.a. (Davis, 1993). Thus, even the insurance industry recognised that it was not in the best interests of the low paid to take out personal pensions and there was increasing public awareness that personal pensions were not a feasible option.

The reforms of the Thatcher/Major years represented a significant deregulation of the pensions market. First of all, from 1988 it was no longer compulsory for an employee to join their employers pension scheme. Secondly, restrictions on Personal Pensions were reduced. Under the 1995 Finance Act, an annuity no longer had to be purchased on the date of retirement. An income could be drawn from the pension fund and the obligation to purchase an annuity did not come into force until the age of 75.

What had been the most important form of regulation – contracting-out - was also reformed. The obligation to provide a Guaranteed Minimum Pension was abolished. From 1997, occupational schemes had to demonstrate that they could offer benefits that were broadly equivalent to SERPS (Pensions Act, 1995: Blake, 1997, p. 226). A further major act of de-regulation was ending the obligation for occupational schemes to finance part of the inflation index once the pensions were in payment (Pensions Act 1997). In order to contract out of SERPS occupational schemes had to index the Guaranteed Minimum Pension up to an inflation level of three per cent. But the 1995 Act abolished the Guaranteed Minimum Pension and required occupational schemes to index the whole pension to a maximum of five per cent. In addition, the responsibility for certifying that occupational schemes meet the new standards shifted from the Occupational Pensions Board which was located within the government department – the Department of Social Security – to the scheme’s professional advisers (Ward, 1999 p. 64.)

In response the Maxwell case, there was a reform to improve the security of pension fund assets through the creation of a compensation fund, a Minimum Funding Requirement and a Statement of Investment Principles (Pension Act 1995). However, there was no regulation to prevent the mis-selling of personal pensions. There was no requirement to demonstrate that shifting from an occupational scheme to a personal pension should be in the best interests of the individual. In addition there was no restriction on the charges that could be imposed by those marketing personal pension products. The idea was that market forces would ensure price competition.

New Labour - New Pensions?

Labour's policy towards state pension provision indicates how far the party had adapted to the legacy of past policy when it came to office in that the reversal of Conservative policy was no longer perceived as feasible. However, it also indicated a departure in traditional Labour thinking regarding the institutions and organisations that should be used to deliver welfare provision. Conservative policy paved the way for the Labour party to question the role of state provision as either the most effective or efficient method of delivering security in old age. Instead the party adopted an innovation which owed a great deal to one of their leading thinkers on welfare - Frank Field (later the Minister for Welfare Reform) who advocated a new innovation - stakeholder pensions – introduced in October 2001. Stakeholder pensions are aimed at those working in a firm that does not provide an occupational pension and the self-employed, based on the conviction that personal pensions do not meet their needs or offer good value for money. They can be used to contract out of the State Second Pension

At first, the Labour party was committed to increasing the basic state pension, the restoration the indexation link to earnings and restoring the value of the earnings related tier (SERPS). However, by 1996, these commitments were abandoned. The cost of restoring the level of pension entitlement was perceived to be too high. The future of pension provision caused some dissension in the Party and as a result the manifesto commitments were vague promising a review of pension provision.

The result of the deliberations has been the development of a scheme which retains the basic state pension increased in line with prices, and established a guaranteed income, substantially more generous than current levels of income support which, it is hoped, will rise in line with increases in national average earnings. The earnings-related second tier is to be gradually phased out and replaced with a State Second pension which will eventually become flat rate like the basic pension.

At the heart of the reforms, however, is the launch of stakeholder pensions in which it is envisaged that funded pension schemes will be provided by the employer, a financial service

company or a collective organisation. The Government claims that this scheme will combine the low overheads and high security of occupational schemes, with the flexibility of personal pensions. They are designed to help those on middle incomes earning between £9,000 and £18,500 per annum. The scheme will be low cost because employers are not required to provide an occupational scheme, but instead provide access to a stakeholder scheme and collect contributions via the payroll. Independent trustees should ensure the interests of scheme members are protected. The government estimates that about five million people will take up this option (Cm 4179, 1998). Stakeholder pensions will operate on a money purchase basis, with the same restrictions. On retirement, twenty-five percent of the fund may be taken as a tax free lump sum, while the remaining fund may be used to buy an annuity or provide pension income by way of a drawdown facility until age 65 when an annuity must be purchased with the remainder of the assets in the fund (Blake 1997 p.223). They have to meet minimum standards regarding the charging structure and level of charging: minimum contribution levels; and offer contribution flexibility and transferability (Blake, 1997, p. 230). In addition, unlike personal pensions, they have to be established under trust law. The Occupational Regulatory Authority, the Ombudsman and the Financial Services Authority regulate them under the provisions of the 1995 Pensions Act.

Regulating Private Sector Pensions:

The preceding discussion has focused on the interplay public and private sector provision. We now turn to the mechanisms for regulation, some of which have emerged in the 1990s and others which have a longer history. There are four principle sources of regulation:

Contracting out conditions (discussed above)

Trust Law

Taxation Policy

Regulatory authorities

Since there are a range of tax advantages available to pension schemes, the Inland Revenue approves private pension schemes. This is not done from the perspective of regulating pension quality, but from the desire to prevent tax avoidance. Their rules focus on the maximum benefits that are available and the maximum level of funds which can be accrued

over time. The Inland Revenue are involved at the point when a pension scheme is set up, or when the rules are being amended.

Trust Law is used to separate pension arrangements from the employers business. It is extremely expensive for an individual to invoke trust law as a way of enforcing their rights. In 1991, a Pensions Ombudsman was appointed to adjudicate cases where trustees may have breached trust law or been guilty of mal-administration. The work of the Ombudsman concerns re-dressing individual grievances. However, in a number of cases there has been examination of the way trustees have behaved in relation to the pension scheme as whole. In particular, there have been a number of cases that investigated the use of surplus funds (Ward, 1999, p. 64-65).

The Registry of Occupational Pension Funds was set up in 1991 to collect all annual reports and pension scheme accounts. However, this registry was to be a public document, and there were fears that this would attract corporate "asset strippers" who would look for pension fund surpluses and then bid to take over companies. As a result this legislation was never enforced and the Register was used as a tracing service.

However, in the aftermath of the Maxwell affair, the Goode Committee (HMSO, 1993) began an extensive review of the framework of regulation that existed. The report criticised the complexity of existing regulation and the way in which it did not resolve competing policy objectives. It found that the interests of scheme members were not adequately protected. Some aspects of regulation that the committee believed should apply to all schemes were only operating in the case of earnings related schemes. There was further concern about the limited scope of solvency requirements and no compensation scheme for members where the employer becomes insolvent.

The array of legislation – over thirty statutes and one hundred statutory instruments – subordinate legislation, memoranda, and practice notes meant that, in the view of the Goode committee there was no clear set of legal rules which set out the rights and responsibilities of pension schemes and their members.

The Goode committee proposed to retain trust law as the basic legal framework, and made a range of recommendations relating the management of schemes, the role of trustees, financial solvency requirements and the settlement of internal disputes. Crucially, they proposed that there should be a statutory authority with overall responsibility for the supervision and enforcement of legal responsibilities. Without this the committee believed a new legal framework would be compromised.

The duties of the regulator were to be

- Registering schemes
- Monitoring schemes, enforcing compliance and legal requirements, including rules relating to trustees, minimum solvency and disclosure.
- Intervening in scheme administration where the scheme assets appear to be in jeopardy
- Receiving and investigating complaints of impropriety in the management of pension schemes or the conduct of trustees
- Disqualifying from acting in the management of an occupational pension scheme those have shown themselves unfit, and maintain a public register of those who had been disqualified
- Monitoring schemes that were being wound up or would require them to be wound up (para.4.19.23 HMSO 1993).

The Pensions Act of 1995 set out a list of reforms that would regulate occupational schemes

- Members of occupational schemes are able to nominate a minimum of one third of the trustee of that scheme
- There is a minimum funding requirement for the funding of most final earnings schemes. The actuary must monitor this on behalf of the trustees. If funding is falling short, the trustees must arrange with the employer to rectify this.
- There must be a written schedule of contributions, and the date the contributions are made. Contributions deducted from the employee must be paid over within 14 days. Unpaid contributions are a debt on the employer

- Schemes must have a statement of investment principals setting out how they intend to meet the Minimum Funding Requirements, their attitude to risk and diversification, how they will obtain advice and monitor investments.
- There are new requirements for record keeping the appointment of advisors, the running of trustees meetings and the setting up of a disputes procedure.

The 1995 legislation created a new regulatory body, the Occupational Pensions Regulatory Authority (OPRA). However, it is not the type of body that was recommended by the Goode committee. The Goode committee envisaged that the regulator would provide a structure for comprehensive monitoring. Reports and accounts would be sent to the regulator and any delay in providing information would be regarded as an indicator of a potential problem. Likewise, if the regulator was able to discern qualifications in the reports of the auditors and the actuaries, they would be alerted to possible difficulties which might deserve further investigation. However, the Government argued that most of the 150,000 schemes were well run and that this level of regulation would be burdensome and undesirable (House of Lords, 1995). As a result, OPRA does not set national standards which it then monitors to ensure compliance. Those associated with pension schemes, such as auditors and actuaries report non-compliance. In effect, the auditor and actuary has been given a duty to "whistle-blow" if they believe any person associated with the pension scheme is failing to comply with the law. Although, OPRA has the authority to write to a random selection of schemes to ask for evidence that they are complying with the law. OPRA has the power to appoint and remove trustees, set civil penalties, wind-up schemes, impose fines on employers and trustees, and order restitution. Unlike the Financial Services Authority, it does not make its own regulations, and therefore does not have the power to "waive" regulations.

Although, the Regulator is not as strong as recommended by the Goode committee, the legislation has gone a long way towards codifying and clarifying regulation. However, regulation of pensions is still fragmented and to a certain extent inconsistent. The regulation of final salary defined benefit schemes is far more advanced than that of defined contribution schemes. Hence, the regulation for the Personal Pension market is more relaxed. This

might lead to a change in employers' preferences away from final salary schemes. Moreover, regulation is divided between the Financial Services Authority, OPRA and the Pensions Ombudsman creating something of a maize of regulators.

Conclusion

The provision of private pensions is a voluntary activity. If the burden of regulation becomes too onerous, the incentive to provide private provision becomes less attractive. However, the UK's pension arrangements are heavily reliant on the private sector, and both the Labour and Conservative parties have encouraged further increases in private provision. Hence the "regulation/risk" dilemma is acute in the British context. The greater the population dependent on the private sector, the more important it is to deliver high quality and reliable benefit systems. However, the dependency on the private sector creates a powerful interest group. The development of regulation is a matter for negotiation rather imposition. In practical terms, Government ministers understand that they have established a relationship of dependency on the private sector, and, as a result, regulation is viewed in terms of what is perceived as feasible for the private sector to provide. We can illustrate this by looking at the history of "contracting-out" arrangements. The liberal nature of these arrangements combined with a low-level of state provision caused the expansion of the private sector in the 1960s. In the 1970s, the state was prepared to under-write the private sector in order to achieve partnership in pensions delivery. Many commentators believe that OPRA's powers should be stronger, as recommended by the Goode committee, and at the moment a review of this issue is taking place (due to report in June). Equally, there is still asymmetry in the regulation of final-salary schemes and defined contribution Personal Pensions.

Moreover, de-regulation has brought other issues to the fore. Numerous companies with traditional occupational schemes based on final salary have been closing these schemes and replacing them with defined contribution schemes. There have been vociferous complaints about the Chancellor's 1997 budget which abolished some of the tax relief on pension funds. Recently, a new accounting standard - FRS 17 - has forced firms to show their pension liabilities in their accounts, and has been used as a justification for winding up final salary schemes. At the same time, there are growing fears about the viability of defined

contribution schemes. Most recently, pension experts have been advising certain employees to contract back into SERPS. Since the beginning of the year, the government has faced a great deal of pressure on this issue. The intensity of political debate has implications for developing a regulatory framework. The government seems caught between the proverbial "rock and a hard place" because increasing regulation is likely to provoke a back-lash from the private sector - failing to act is likely to further damage public confidence.

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