

EXPLANATORY MEMORANDUM TO
THE SOCIAL SECURITY REVALUATION OF EARNINGS FACTORS ORDER
2017

2017 No. 287

1. Introduction

- 1.1 This explanatory memorandum has been prepared by The Department for Work and Pensions and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

- 2.1 This Order is being made to ensure that earnings factors relating to National Insurance contributions for past tax years, used in the calculation of additional State Pension and Guaranteed Minimum Pensions, maintain their value in line with the movement in average earnings.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

- 3.1 None.

Other matters of interest to the House of Commons

- 3.2 As this instrument is subject to negative resolution procedure and has not been prayed against, consideration as to whether there are other matters of interest to the House of Commons does not arise at this stage.

4. Legislative Context

- 4.1 Under section 148 of the Social Security Administration Act 1992¹, the Secretary of State is required, in each tax year, to review the general level of earnings in Great Britain. If there is an increase during the review period, he is required to make an order to increase the earnings factors for past years used in the calculation of additional State Pension (State Earnings Related Pension (SERPS), State Second Pension (S2P)) and Guaranteed Minimum Pensions (GMPs) so that they maintain their value relative to earnings growth. This instrument (referred to in this Memorandum as the “Revaluation Order”) is being made to fulfil this requirement.

5. Extent and Territorial Application

- 5.1 The extent of this instrument is Great Britain.
- 5.2 The territorial application of this instrument is Great Britain.
- 5.3 Subject to Ministerial agreement, the Department for Communities in Northern Ireland will make corresponding provisions for Northern Ireland.

[1http://www.legislation.gov.uk/ukpga/1992/5](http://www.legislation.gov.uk/ukpga/1992/5)

6. European Convention on Human Rights

- 6.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation no statement is required.

7. Policy background

What is being done and why

Additional State Pension

- 7.1 For the purposes of additional pension, ‘earnings factors’ essentially represent the amount of earnings on which relevant National Insurance contributions have been paid or treated as paid over a person’s working life from 1978/79 onwards. They are derived from earnings upon which primary Class 1 contributions have been paid or treated as paid, and from Class 2 and Class 3 contributions paid². For years from 2002/03 to 2015/16 (the last year of additional State Pension accrual) additional pension accrued on primary Class 1 contributions only. Carers and disabled people entitled to certain benefits are treated as having an earnings factor for these purposes.
- 7.2 The earnings factors derived for each year from 1978/79 (when the additional State Pension was introduced) to 2015/16 are revalued annually in line with the movement in average earnings. This annual revaluation exercise allows earnings factors derived from historic earnings to be restated at current values as part of the calculation of an award of additional State Pension under both SERPS and S2P. Once in payment, additional State Pension is up-rated annually in line with the general increase in the level of prices.
- 7.3 Since 6 April 2016, the Revaluation Order also provides the percentage used to revalue flat-rate amounts of S2P accrued in tax years 2012/13 to 2015/16 which were formerly revalued by way of a separate Order (the Social Security Pensions (Flat Rate Accrual Amount) Order). The last such Order reset the flat-rate amount at £93.60 for 2015/16.³ From 6 April 2016, flat-rate amounts are increased by the percentage specified for 2015/16 in the Schedule to the Revaluation Order.⁴
- 7.4 On 6 April 2016, the old two-tier State Pension of basic and additional State Pension was replaced by a new State Pension for people reaching State Pension age on or after that date. The new State Pension is based on a flat-rate amount (1/35th of the full rate of new State Pension) for each qualifying year of paid or credited National Insurance contributions from 6 April 2016 onwards, up to a maximum of 35.⁵ This means that there are no further accruals of additional State Pension after 5 April 2016. However, new awards of inherited additional State Pension will still be possible after that date, payable either as part of an old State Pension to a surviving spouse or civil partner who had reached State Pension age before 6 April 2016, or (until 5 April 2017) as part

² Class 1 National Insurance contributions are paid by employed earners. Class 2 are paid by the self-employed. Class 3 National Insurance contributions are voluntary contributions to make up gaps in a person’s National Insurance contributions record.

³<http://www.legislation.gov.uk/uksi/2015/185/contents/made>

⁴ See Article 2 of the Pensions Act 2014 (Consequential and Supplementary Amendments) Order 2016, S.I. 2016/224 <http://www.legislation.gov.uk/uksi/2016/224/contents/made>

⁵ Contributions made before that date are recognised in the form of a “starting amount”, comprising the higher of the calculations of the person’s State Pension as at 6 April 2016 under the old and new rules. If the starting amount is less than the full rate of new State Pension at that date (£155.65), it can be increased, up to a maximum of the full rate, by 1/35th of the full rate for each qualifying year gained from 6 April 2016.

of Widowed Parent's Allowance to a surviving spouse or civil partner widowed under State Pension age.

- 7.5 Where the deceased spouse or civil partner had reached, or would have reached, State Pension age under the new State Pension rules, the survivor's inherited additional State Pension will be calculated from the deceased's earnings factors and flat-rate accrual amounts of S2P up to and including 2015/16, revalued to the tax year immediately before the tax year in which they died or, if later, reached State Pension age. This is to ensure that earnings growth beyond 6 April 2016 is reflected in the survivor's pension, as it would have been had the new State Pension had not been introduced.

Shared additional pension

- 7.6 Where a pension sharing order has been made by the Courts in respect of a person's additional State Pension, this creates a state scheme pension credit for the party who will have State Pension credited to their account (the transferee), and a state scheme pension debit for the person whose additional State Pension is to be shared (the transferor). A state scheme pension debit becomes a weekly deduction from the transferor's State Pension when they reach State Pension age or, if later, the effective date of the pension-sharing order. State scheme pension credits give rise to a weekly State Pension for the transferee which becomes payable from the later of State Pension age or when the pension-sharing order takes effect. Where the share order takes effect before the start of the final tax year prior to State Pension age, the debit or credit, as applicable, needs to be revalued. The revaluing percentage is the percentage specified in the last Revaluation Order to come into force before State Pension age for the tax year in which the share order takes effect.
- 7.7 From 6 April 2016, additional State Pension will still be shareable where either the transferor reached state pension age before 6 April 2016 or the divorce or dissolution proceedings began before that date. This means that provision to revalue the ensuing old state scheme debit and credit is therefore needed where the pension-sharing order takes effect in tax years starting on or after 6 April 2016. This provision is made by paragraph 2 of Schedules 8 (credits) and 10 (debits) of the Pensions Act 2014.⁶ The percentage specified in this order for tax year 2016/17 will be the revaluing percentage for old state scheme debits and credits created in tax year 2016/17, and will apply where the transferor (in the case of the debit) or transferee (in the case of the credit) reaches State Pension age in tax year 2018/19.

Guaranteed Minimum Pension

- 7.8 For the purposes of GMPs (the pension paid in lieu of additional pension by an occupational pension which was contracted-out of SERPS) only earnings factors for the years 1978/79 to 1996/97 are relevant as the contracting-out arrangements changed from April 1997. GMPs are based on earnings factors on which primary Class 1 contributions were paid. Other than where an individual leaves a formerly contracted-out scheme before GMP pensionable age (60 for women, 65 for men), section 16 of the Pension Schemes Act 1993⁷ requires the earnings factors to also be

⁶ <http://www.legislation.gov.uk/ukpga/2014/19/contents/enacted>

⁷ <http://www.legislation.gov.uk/ukpga/1993/48>

revalued using the relevant order under section 148 of the Social Security Administration Act 1992.⁸

- 7.9 This order deals with revaluing GMP accruals in the period before the pensioner reaches pensionable age, revaluing these in line with earnings growth. A separate order, “The Guaranteed Minimum Pensions Increase Order”, provides for uprating those GMPs already in payment.

Revaluation Period and Increase

- 7.10 Revaluations are calculated by reference to the change in earnings over the period of 12 months up to the end of September. This allows sufficient time for the resulting Order to be made before the beginning of the tax year in which it is to apply.
- 7.11 During the period between September 2015 and September 2016 the Office for National Statistics’ Average Weekly Earnings statistics September year-on-year change (non-seasonally adjusted, including bonuses)⁹ showed that average earnings in Great Britain increased by 2.6%.
- 7.12 The Revaluation Order accordingly provides for earnings factors for 2016/17 and earlier tax years to be increased by cumulative percentages which reflect this increase and in addition, the increases provided for by previous Orders.

Consolidation

- 7.13 As this instrument does not amend other instruments the question of consolidation does not arise.

8. Consultation outcome

- 8.1 There is no statutory duty on the Secretary of State to consult on this instrument. The Department does not consider informal consultation is appropriate in this case, as this is a technical order which gives effect to a statutory requirement specified in primary legislation.

9. Guidance

- 9.1 Information and guidance on the additional State Pension and Guaranteed Minimum Pensions is published by the Department on www.gov.uk.

10. Impact

- 10.1 There is no new impact on business, charities or voluntary bodies.
- 10.2 The Order imposes no new costs on the public sector.
- 10.3 An Impact Assessment has not been prepared for this instrument as it delivers a pre-existing statutory requirement.

⁸ Where individuals leave before GMP pensionable age, a scheme may choose to revalue the GMP by a fixed rate, as provided by section 16(2) and (3) of the Pension Schemes Act 1993. The fixed rate method is based on an actuarial estimate of future earnings increases which is reviewed periodically and updated as appropriate based on advice by the Government Actuary’s Department.

⁹ Average weekly earnings by sector at <http://www.ons.gov.uk/ons/rel/lms/labour-market-statistics/december-2016/table-earn02.xls>

11. Regulating small business

- 11.1 The Order applies to formerly contracted-out occupational pension schemes, but has negligible administrative impact on them.

12. Monitoring & review

- 12.1 There are no plans to monitor the effect of this Order. There is a statutory requirement to ensure the additional State Pension and GMPs maintain their value relative to earnings growth.

13. Contact

- 13.1 Paul Needham at the Department for Work and Pensions (Telephone: 0113 2324949 or email: paul.needham@dwp.gsi.gov.uk) can answer any queries regarding the instrument.