National Audit Office

Report
by the Comptroller
and Auditor General

Department for Work & Pensions

Introduction of the new state pension

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Key facts

£89bn

spending on state pension in 2015-16

407,000

people forecast to claim the new state pension in 2016-17

2.1m

people have checked their state pension forecast since September 2014

0.5% of GDP	forecast reduction in spending on state pension and pensioner benefits in 2060, compared to forecast of expenditure under the previous state pension
£2 billion	forecast increase in net national insurance contributions in 2016-17 from introducing the new state pension in April 2016, one year ahead of the date originally proposed
50%	fewer people in 2030 will be eligible for Pension Credit than now
73%	of people who reach state pension age in 2030 will be better off under the new state pension
76%	of people who reach state pension age in 2060 will be worse off under the new state pension
77%	of people within 10 years of state pension age are aware of state pension changes
18%	of working age people know how much their state pension is likely to be

Summary

1 On 6 April 2016, the government introduced the new state pension. From this date, everyone who reaches state pension age will have their entitlement calculated using the new rules. The Department for Work & Pensions (the Department) calculates each person's entitlement based on qualifying years of national insurance contributions. The Department's transitional arrangements ensure that – for everyone who qualifies for the new state pension – their contributions to 6 April 2016 will be worth at least as much as they would have been under the previous system.

2 Introducing the new state pension lessens the long-term cost to government. In 2015-16, the state pension and pensioner benefits cost £117 billion (6.3% of GDP), including £89 billion on the state pension itself. The Department forecasts that in 2060 pensioner benefits will have risen to 7.6% of GDP, around 0.5% of GDP less than had the previous system continued. The government is also increasing the national insurance contributions that some employers and employees pay. It expects to raise an additional £2 billion in contributions in 2016-17.[1]

3 Because spending on state pension will increase at a slower rate, most people will receive less than previously projected in the long term. In 2060, 76% of people will receive, on average, £15 a week less. But people will be affected very differently depending on their circumstances. For example, self-employed people, low earners and some people who took time out of the labour market to look after children are likely to get higher rates of state pension. But other people may lose out; for example, those who do not have the minimum number of qualifying years, and some people who were in contracted-out defined benefit pension schemes who are close to state pension age in April 2016.

4 While the new state pension reduces direct government support, it aims to encourage people to save for their retirement by simplifying the rules and letting them know what they will get from the state. The government's intention is that this will help people to plan for retirement from a younger age and to save in other ways. For example, while the new state pension eliminates the earnings-related additional state pension entitlement, the Department is expanding private saving through automatic enrolment of workers into employers' pension schemes.

1 The government forecasts the annual gross increase in national insurance contributions to be £5 billion. The cost to government, as an employer, of increasing national insurance contributions is £3 billion.

5 Two departments are responsible for processing state pension claims:

- the Department pays the state pension and sets wider pensions policy. It has been responsible for communicating the changes and ensuring people receive the payments to which they are entitled.
- HM Revenue & Customs (HMRC) collects national insurance contributions and is responsible for calculating each person's initial state pension entitlement. HMRC is working with occupational pension scheme providers to ensure records of people's employment and pension history are correct.

Scope of this report

6 The effective introduction of the new state pension is important in its own right and as a core part of wider pension reforms. The new system changes the way state pension is calculated. People rely on government to get this calculation right and administer payments efficiently. More broadly, as the government encourages people to take greater responsibility to save privately for their retirement, it needs to increase awareness of likely retirement incomes and support long-term retirement planning. This report therefore covers:

- the objectives of the new state pension;
- the Department's implementation of the new state pension;
- the Department's processing of new state pension claims; and
- the effectiveness of the communication campaign.

7 This is one of a series of National Audit Office reports tracking the progress of pension reforms and wider pension liabilities.[2] We plan to produce further reports to evaluate the Department's progress in implementing pension reforms.

Key findings

Implementing the new state pension

8 **The Department introduced the new state pension one year ahead of the date originally proposed.** The 2013 white paper stated that the government would not introduce the new state pension before April 2017.[3] In March 2013, the government announced it would bring this forward to April 2016, introducing higher national insurance contributions one year earlier than originally planned (paragraphs 2.2 to 2.4).

2 Comptroller and Auditor General, *Evaluating the government balance sheet: pensions*, Session 2016-17, HC 238, National Audit Office, June 2016. Comptroller and Auditor General, *Automatic enrolment to workplace pensions*, Session 2015-16, HC 417, National Audit Office, November 2015. Comptroller and Auditor General, *Whole of Government Accounts*, May 2016. Comptroller and Auditor General, *Government interventions to support retirement incomes*, Session 2013-14, HC 536, National Audit Office, July 2013.

3 Department for Work & Pensions, *The single-tier pension: a simple foundation for saving*, Cm 8528, January 2013.

9 **The Department met its deadline by making the minimum necessary changes to its IT systems.** It recognised the risks of introducing the new state pension. From July 2013, it focused on adapting existing IT systems and deferred the development of a more ambitious digital solution that offered operational efficiencies and new customer services. The Department completed the system changes to allow the uninterrupted payment of state pension from the 'go-live' date in April 2016. It performed well against its identified critical success factors and the project was within budget, costing £57 million up to March 2016 (paragraphs 2.5 to 2.8 and 2.10).

10 **The Department has not yet introduced a new digital claims service.** It originally intended digital services to be available from April 2016. These would allow people to check a statement of their state pension entitlement, make a claim and report changes in their circumstances. The Department prioritised the digital pension statements service and introduced this in February 2016. The new digital service for making a claim is now due in April 2017 but the change of circumstances service is not expected before 2018 (paragraph 2.9).

11 **The Department is now expecting to make much smaller operational savings than originally planned from the new state pension.** It reduced the expected operational savings from £341 million to £73 million. The Department's decision to de-scope the project accounted for £157 million of this reduction. It reduced benefits by a further £80 million to reflect lower than expected efficiency savings. The costs of implementing the project are now expected to exceed the operational benefits by £25 million (paragraph 2.11).

Processing new state pension claims

12 **The departments are likely to maintain the accuracy of state pension payments.** The calculation of entitlement is based on the same national insurance data as the old system. The rule changes make the calculation simpler. HMRC routinely checks the completeness of national insurance contributions. Both departments comprehensively tested the changes to the systems for processing state pension claims, and the Department's quality checking shows low levels of error on new state pension payments. The two departments have worked together to identify risks to data quality, but the flow of data between the two departments for new state pension is not supported by a formal data assurance agreement. This increases the risk that future responsibilities for data assurance are unclear (paragraphs 3.2 to 3.9).

13 **HMRC is checking its national insurance data with pension schemes but take-up of the service, and therefore progress, is slow.** The introduction of the new state pension has allowed HMRC to bring forward the reconciliation of records that was previously done at the point of retirement. This will allow HMRC and pension schemes to check the accuracy of their records and provide people with a more accurate initial assessment of the state pension they have built up at April 2016. Pension schemes representing 14.2 million individual memberships (77% of all deferred and pensioner memberships) have registered with HMRC. Initial take-up of the service by pension scheme administrators was slow. By August 2016, HMRC had confirmed just 1.7% of deferred and pensioner memberships. HMRC also forecasts that it will receive 55% more queries than originally expected. It still aims to complete this work by December 2018 but may need extra resources to do so (paragraphs 3.10 to 3.14).

14 **There has been some deterioration in the time taken to process claims.** This relates partly to the introduction of the new state pension but also reflects wider demands on operational staff since April 2016. The Department's performance in processing claims began to recover in August 2016. The Department has previously achieved high levels of customer satisfaction and low levels of under and overpayments in processing state pension claims. Data on performance against these measures will be available in 2017 (paragraphs 3.15 to 3.18).

The communication campaign

15 **The communication campaign raised awareness of the changes to the state pension.** The Department focused on people within 10 years of state pension age and aimed to dispel common misconceptions. Based on our evaluative framework, we found the Department managed the campaign well, continuously monitoring its customer research and adapting its approach. The campaign improved general awareness of the changes to the state pension (paragraphs 4.2 to 4.6).

16 **The Department's attempts to improve people's understanding of their state pension have had limited success so far.** Recognising the variation in people's circumstances and the difficulty of tailoring messages, the Department's campaign aimed to increase people's understanding of their new state pension entitlement. Since September 2014, some 2.1 million people of all ages have checked their state pension entitlement. But in April 2016, 25% of working age people knew how changes to the new state pension will affect them and 18% knew what their state pension was likely to be. Before February 2016, only people within 10 years of state pension age could request a pension statement and these people have a better understanding of how they are affected (paragraphs 4.7 to 4.9).

17 **The Department did not directly contact groups of people affected by the rule changes.** The rule changes mean some people will gain while others lose out. In response to a report by the Work and Pensions Committee, the Department will write to over 100,000 people who are unlikely to reach the minimum number of qualifying years. However, it rejected calls to write to other groups likely to lose out because it could not accurately identify the people affected and did not think contacting people directly was an effective approach. Instead, it sought to reach these groups through its communications campaign. Our recent report highlighted a lack of clear information for people with guaranteed minimum pensions, and that it has been difficult for them to find information on how the reforms affect them (paragraphs 4.6 and 4.10 to 4.13).[4]

18 **The current new state pension communications campaign is not likely to be a major factor in increasing people's saving for retirement.** One of the Department's objectives of its state pension reform was to prompt people to take action and plan for their retirement from a younger age. There is no evidence yet that the new state pension has encouraged people to save more for their retirement. The Department recognised that the campaign on its own was unlikely to shift behaviours substantially in the short term. Its approach to changing behaviours largely relies on the success of automatic enrolment in increasing savings, rather than on simplifying the state pension (paragraphs 4.14 to 4.17).

Conclusion on value for money

19 The Department has successfully managed the introduction of the new state pension. It introduced the changes one year ahead of its original plans, allowing the government to increase national insurance revenues and bring forward long-term changes to improve the sustainability of state pension spending. In implementing the programme, the Department reduced risks by decoupling plans for new digital services and working with HMRC to conduct extensive testing of systems used to calculate entitlement. The cost of the programme is within budget and operational performance has largely been maintained. So far, the Department's implementation of the new state pension represents value for money.

20 Pensions reforms are long-term endeavours and the Department will need to tackle two important areas to achieve value for money as the reforms develop. First, the Department's focus on policy delivery has reduced the scope for operational savings and postponed the introduction of digital services. The Department has yet to reintroduce its original plans for a more fundamental digital transformation of pension administration. Second, achieving the longer-term objectives of the new state pension will depend on how it interacts with wider reform of the pensions system. The new state pension tackles concerns about state pension affordability but increases the need for people to make their own retirement provision. It is not yet clear whether the simplification of the state pension will improve understanding of retirement savings and how this will affect wider pension reforms supporting private saving.

4 Comptroller and Auditor General, *The impact of state pension reforms on people with Guaranteed Minimum Pensions*, Session 2015-16, HC 907, National Audit Office, March 2016.