Scottish Independence - Pensions

Introduction

Having attended the lively debate organised by Andrew Sloan of the Scottish Business group I came away feeling that it was an interesting and worthwhile exercise and certainly got people thinking about both Scotland and the UK.

There were 4 main questions which came up which I wanted to look at further.

How UK pensions would be paid in and Independent Scotland and the answer given was that UK pensions were funds already guaranteed by the Government, so would be paid from the UK in future. I thought it as a little more complicated than that and warranted more investigation and contemplation on my part.

It was also said that UK State pension levels are near the bottom of the league table which is true, but this is already changing in 2016 which brings significant increases and so is maybe an unfair reflection.

It was also suggested that the Scottish State Pension Age would reduce to 63 due to its poorer life expectancy. Whilst mortality is an obvious factor, again, I didn't feel it would be quite as simple as that.

Finally, the question arose that if half the pension were payable in UK currency and half in Scottish currency, how would it work. It was stated it would be paid through funds already there. My thoughts were similar to question one in that they are not funded, but that the answer also related to currency choice.

As there were only 'Yes' advocates answering questions, I can only respond to their points and respect their ability to answer a wide range of questions in as concise a way as possible, with each question being very complex in itself. Indeed, 'Yes' can only answer the questions in many ways as the 'No' remains the same. Everything is very much down to negotiation as nothing is hard and fast.

Credentials

Why am I responding? I worked in the UK pensions industry since 1985 and offshore in Thailand since 2009. I hold the UK qualifications the Diploma in Retirement and Pensions and the Advanced Diploma in Pensions. I therefore have a good idea about the issues that surround UK pensions and pensioners and have used that to relate to Independence repercussions.

Current UK position

The position of State and Private Pensions is quite complicated already with a number of changes made over the years and more pending in the UK in 2015 for private pensions and 2016 for State pensions. 'No' vote retains the current UK position, whereas 'Yes' vote allows the new Scottish Government to make changes which therefore need to be paid for.

All UK state pensions are unfunded whereby today's tax payers pay for today's pensioners. With an ageing population, the UK cannot afford to pay at the current rate.

UK Changes

No vote – Changes per current UK model in 2016 currently £113.10 pw increases to estimated £155pw but includes both basic and 2nd (SERPS) pensions. National Insurance for maximum basic pension will increase from 30 to 35 years.
Will increase every year by 2.5 per cent in line with either earnings or prices, whichever is highest.
Age

- Ladies increasing to 65 between 2010 and 2018
- All increase to 66 by 2020
- 67 between 2026 and 2028

UK Government pensions including civil service, armed forces, police, fire-fighters, NHS, universities, teachers and local government pensions are also unfunded and so come from tax payers of today. Each person has a past and future pension promise and this would be an ongoing burden on future tax payers.
'Yes' Vote – Will depend what the new Scottish Parliament decides. However, the current Scottish parliament says they are to keep the State pension promises from the UK based upon past National Insurance history, meaning they will have to pay for it rather than the UK. National Insurance contribution history gives an entitlement to basic and 2nd pensions which is a debt against the Government paying them. The Scottish Government states "There will be agreement between the Scottish and UK governments as to the exact share of pension liabilities to be taken on by the Scottish Government".
The current Scottish Parliament has stated "On the date of independence, people retiring will be entitled to the Scottish State Pension based on years of national insurance credits built up in the UK. From that point onwards, entitlement built up in Scotland will accrue to the Scottish State Pension."
Who would be entitled to a Scottish rather than a UK pension and how and when could this determination be made to affect the cost sharing? This may not be straightforward due to the transient residency and citizenship. Currently NI contributions are paid by residency, so someone having moved between the two countries could either be paid by both or part of the negotiation determining who is entitled to which one and so who should pay for them.

Thailand

Key things which could have an effect on pensioners in Thailand are;

- Amount
- Currency
- Taxation
- Increases

Amount

SNP - Deputy First Minister Nicola Sturgeon

- Match UK State pension increase mechanism for at least the term of the first Scottish Parliament
- Single-tier pension set at a minimum of £160 a week. It is difficult to see this as more than a political figure in being a little more than the UK Government proposed reform, rather than a well thought out and accurately costed amount based upon a new Scotland and the needs of its pensioners.
- Review the State pension age of 67. There has been no guarantee of a reduction only that a review will take place. The assumption is that if Scottish mortality is higher, pensions don't need to be paid for so long and so could be started earlier. With the rest of the world already reviewing and increasing state pension ages due to the huge burden on tax payers, it seems unlikely that any scenario would cause Scotland to go against the trend without putting a huge future burden on its ability to meet the future liabilities.

www.aimspi.com
AIMS PI (Thailand) Limited, Company Registration Number 0105557065708
388 Exchange Tower, 29th Floor, Sukhumvit Road, Klongtoey Sub district, Klongtoey District, Bangkok, 10110, Thailand
Tel: +66 (0) 847376036 Fax: +66 (0) 21049101

Currency

Thai residents already have a currency risk for income from State and private UK pensions. Depending on the Independent Scotland's currency this may affect the value of the pension income.

- Monetary Union – SNP says best option but Westminster says no. All 3 leaders of UK main parties have dismissed this option. SNP hints if they do it will default on debt accrued at the time of the split. The UK could offset against many things during their period of bargaining, defence, civil service etc. Future Scottish borrowing at risk if they did so. NO CHANGE
- Use pound unofficially. No ability to print money and so affect lending and interest rates etc., but allows business to flow as does now. NO CHANGE as long as Scotland can get hold of enough currency to pay it out. I assume Scottish versions of the notes would no longer be valid?
- Euro – Tie into a different currency mechanism which is more volatile than Sterling. No guarantee of membership of EU or exchange rate mechanism. SNP say no as a solution. AFFECT FROM DIFFERENT EXCHANGE CURRENCY
- New currency – SNP say no as a solution. Large financial burden to run. AFFECT FROM DIFFERENT EXCHANGE CURRENCY

There does not seem to be any workable answer on the table at the moment as the 'Yes' position seems to be that the UK politicians will back down and allow monetary union and it is no more than brinksmanship to sway the vote, but what if it is not? If David Cameron does a U turn on this position after the 'Yes' vote, this would seriously impact his credibility.

AIMS Pensions and Investments

Taxation

All UK pensions including both private and state are treated as earned income as if they had been earned in the UK in the tax year of receipt and are therefore subject to income tax. Current UK tax rates and allowances for 2014/15 are;
Tax Free Allowance - £10,000 (increasing up to £10,660 for older) which reduces for income over £100,000
Basic Rate – 20% to £31,865
Higher Rate -40% to £150,000
Additional Rate – 45% over £150,000
Scottish Government has not quoted a rate, but said "The Scottish Government's White Paper on independence sets out plans to create a distinct Scottish system, which it says would be "less cumbersome and less open to avoidance", taking advantage of new technology.
Revenue Scotland, which is being set up to collect taxes devolved in the Scotland Act 2012, will form the foundations of the new system. The Government proposes a "transition phase" after independence where taxes will continue to be collected through existing HMRC systems, with the Scottish system collecting all taxes "as quickly as possible". General statement that taxes will not increase. AFFECT UNKNOWN

Increases

Current UK pensions are subject to increases in the UK and for those living in some countries abroad. However, in many countries such as Thailand there are no such increases and so the pension is restricted to the amount payable at the date of leaving the UK. This was taken to the EU court and the UK Government won. I can find no comment in relation to this issue so it would be up to any future Scottish Parliament to determine whether this was fair and if not whether the additional cost of providing it could be met. The current UK rules relate to its EU obligations and its tax treaties with other countries whereby some have reciprocal arrangements relating to pensions and some don't. Presumably an independent Scotland would have to renegotiate any such international treaties and make decisions on a country by country basis?

www.aimspi.com
AIMS PI (Thailand) Limited, Company Registration Number 0105557065708
388 Exchange Tower, 29th Floor, Sukhumvit Road, Klongtoey Sub district, Klongtoey District, Bangkok, 10110, Thailand
Tel: +66 (0) 847376036 Fax: +66 (0) 21049101

Eligibility

The question is having accrued a UK pension, who will be eligible for a Scottish Pension and who remains to claim a UK one. The future is clear, if you work in Scotland; you pay Scottish NI and accrue credits to a Scottish State Pension. For past service, it may either relate to residency or citizenship. The Scottish Government white paper says "British citizens habitually resident in Scotland on independence will be considered Scottish citizens. This will include British citizens who hold dual citizenship with another country. Scottish born British citizens currently living outside of Scotland will also be considered Scottish citizens. The Scottish Government will allow dual citizenship. It will be for the rest of the UK to decide whether it allows dual UK/Scottish citizenship". This begs the question for past pension accrual, for someone who chooses joint citizenship, who pays their pension? Could this lead to people choosing their citizenship based upon the size of pension they receive and could this lead to a larger burden than either Government anticipates?

Other Pensions

UK pensions have changed significantly over the years with a move away from final salary related employer schemes which were great for employees but created an open ended liability for employers. The UK like other similar economies has move to Money Purchase arrangements which are more like bank accounts and has gradually eroded the value of private pensions by significantly cutting back tax relief. We currently have a UK and EU wide transfer mechanism where someone moving employers can move their pension with them or they can make their own private funding. Any Scottish legislative changes would no doubt affect this position and so rules would need to be worked out between both Governments.

www.aimspi.com
AIMS PI (Thailand) Limited, Company Registration Number 0105557065708
388 Exchange Tower, 29th Floor, Sukhumvit Road, Klongtoey Sub district, Klongtoey District, Bangkok, 10110, Thailand
Tel: +66 (0) 847376036 Fax: +66 (0) 21049101

Conclusion

A yes vote means a long negotiation between both Governments to see who takes on the burden of the pension promises of current UK State and private government funded pension schemes and to what extent.

The new Scottish Parliament then needs to set a manageable budget and taxation system to manage the expenses relating to the amount and increases in current and future pensions.

For an existing or future pensioner there is uncertainty as to levels of taxation and the currency. Exchange rates are not clear and so the effect on continued buying power is unknown despite the promises of meeting pensions already accrued and increases on such. However, there is uncertainty in anything new and so the question is whether there is sufficient belief in the numbers to meet the promises.

It is up to the voters to decide whether the economic projections set out by the 'Yes' campaign are reasonable or whether the 'No' campaigns radically different projections are more accurate.

Under a 'No' vote it is clear change will happen as well as Westminster indicates further devolution for Scotland.

You decide.

Paul Wyatt
Managing Director
AIMS PI (Thailand) Limited

www.aimspi.com
AIMS PI (Thailand) Limited, Company Registration Number 0105557065708
388 Exchange Tower, 29th Floor, Sukhumvit Road, Klongtoey Sub district, Klongtoey District, Bangkok, 10110, Thailand
Tel: +66 (0) 847376036 Fax: +66 (0) 21049101