Index-linked pensions are essential

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Apathy and ignorance used to surround the subject of pensions. Most doctors gave little thought to it even though the final capitalised value of their occupational pensions could often exceed that of their homes. If the same time and effort were devoted to the upkeep of superannuation schemes as is spent on home maintenance, many of the present pension anomalies could have been avoided. But inflation has changed all this. The apathy has now gone and a doctor's pension has become as much of an obsession as remuneration, particularly if he can see retirement approaching. Even so, there are still far too many doctors approaching retirement who only bother to investigate their pensions during the last year of service, when it is far too late to rectify anomalies or purchase additional benefits.

I have heard academics, teachers, members of the armed Forces, and doctors criticise the index linking of pensions, believing that this arrangement is exclusive to the Civil Service, quite unaware that it also applies to their own pensions. In fact, at least five and a half million employees are in occupational pension schemes that provide inflation-proofed pensions; this figure includes the Civil Service, the armed Forces, the Health Service, local government, police, and the nationalised industries, and represents over 20% of the employed population and over 40% of the total number of employees in occupational pension schemes.

Two nations of pensioners

The impact of inflation on pensions has been dramatic. For those employees in the private sector whose schemes have made little or no provision for pension increases to take account of inflation, the effects of the last decade have been severe. Many pensioners who retired during the last 15 years believing that they had earned a pension that would be adequate for their needs in retirement have seen its real value seriously eroded. It is understandable, therefore, that the people who have not shared the benefits of index linking enjoyed by public sector pensioners should feel embittered and direct their anger towards those who have been more fortunate. This public outcry about the differential treatment of pensioners in the public and private sectors led the Government to appoint a committee under the chairmanship of Sir Bernard Scott to inquire into the value of differences in the inflation protection of occupational pensions and the value of relative job security for the purposes of determining public sector pay and other conditions of service. The committee has now reported,¹ concluding that the standard of living of all pensioners should be protected and favouring the extension of index linking to the private sector.

On reflection it is extraordinary that so many private sector employers have shown scant regard for the plight of their pensioners, even though the actual cost of maintaining the real value of their pensions over the past 10 years would not have been prohibitive. But instead of acknowledging that they have a moral obligation towards former employees, most of these employers have preferred to excuse themselves on the

grounds of cost and have been content to allow inflation to reduce arbitrarily the real income of their pensioners. Not until there is general recognition that all employers have an obligation to maintain the value of their pensioners' incomes—at least in line with movements in the pay of their employees—can this anomaly be finally removed. This means that employers will have to attach higher priority to their pensioners than has been the case so far. The excuse that there is insufficient finance in a company to afford the luxury of index-linked pensions is a hollow one. For every organisation it is simply a question of priorities; either pensioners are to be treated on the same terms as existing employees or not. Indeed, it seems that the low priority attached to pensions by private sector employers is only too evident in the low level of employee contribution to their schemes: on average, barely half the level of many public sector schemes.

The Scott Report is important because it seeks to impress on the private sector the need to recognise its obligations. It also suggests how the Government can assist private sector employers to provide index-linked pensions. Since it is not so much the cost of providing pension increases that has been the main deterrent but rather the element of uncertainty about future inflation rates, the Scott Report proposes that index-linked bonds should be issued to cover the liabilities of employers in the payment of pensions.

How much should we pay for index-linked pensions?

The general argument against index-linked pensions is that they are largely financed by the taxpayer and it is unfair that the private sector should be required to help provide a level of benefit that it is unable to afford for its own employees. In the present economic climate such a burden can only heighten the problems facing British industry. Thus, the argument runs, either index-linked pensions should be abolished or public sector employees should contribute in full towards the additional benefits that they receive. Present methods of assessing the value of these additional benefits bear little relation to reality and take no account of the fact that full inflation protection is guaranteed rather than discretionary. The Scott Report, having endorsed in principle the protection of pensioners' incomes against inflation, directs its attention to estimating the true costs of index-linked pensions for public servants.

Any estimate of the value of an index-linked pension depends on assumptions about future returns on pension fund assets and future rates of inflation. Indeed, it is the difference between them, the real rate of return on investments, that is critical to the value of pensions. The committee considered how these factors could be expected to vary in order to establish a reasonable range within which (apart from the circumstances of extreme inflation rates) the employee's contribution could be said to lie. The committee concluded that the employee's contribution for public servants would lie between about 7% and 13½% of pensionable pay. Though these calculations are based on the Civil Service pension scheme, the report suggested that the figures were probably indicative of those that should apply to other public sector schemes. Doctors now contribute 6% of their pensionable salary, whereas for civil servants the notional figure is 7.9%.

An important underlying assumption in these calculations is that, in the last resort, there would need to be some cut-off point beyond which pension increases would have to be restricted. Without such an assumption a valuation of inflation-

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More proposals for London's medical schools

Following the University of London's request for a re-examination of proposals to reduce the overprovision of preclinical teaching in London (15 November, p 1369), the Joint Planning Committee of the Court and the Senate has made another set of recommendations on restructuring medical education in London. The committee recommends that St George's Hospital Medical School should be allowed to increase its preclinical intake as planned to 150; that St Bartholomew's and the London Hospital medical schools should reduce their preclinical intake to 200 subject to cost studies and a decision on siting; that Charing Cross and Westminster Hospital medical schools should merge, with preclinical teaching at Fulham and a clinical entry of 175; and that

the Royal Free School should consolidate at Hampstead. The committee also proposes a joint school of St Mary's, the Middlesex, and University College medical schools linked with two or three postgraduate institutes; to achieve large savings one preclinical school, probably St Mary's, and one clinical school, probably the Middlesex, should close, and the committee recommends that the savings made by this proposal should be estimated. The committee also rejected a proposal to close the preclinical departments at King's College and a suggestion that Guy's, St Thomas's, and King's College Hospital medical schools should form a joint school together with King's College and the Institute of Dermatology, though Guy's, St Thomas's, and the Institute of Dermatology

have already asked to be allowed to form a united school. The committee's proposals go before the Senate on 25 March and the Court on 1 April.

Hospital charges for foreign visitors

Mr Patrick Jenkin told the House of Commons on 12 March that subject to some exceptions the Government proposed to make regulations providing for charges to visitors from abroad for hospital treatment. The new charges would apply to those who were not ordinarily resident in the United Kingdom. Free outpatient treatment at accident and emergency departments would continue and the charges would take into account the various reciprocal arrangements for medical services that the UK had with the EEC and 14 other countries. Exceptions would be made for visiting spouses and dependent children who had settled here. The Secretary of State said that consultations with the Health Service had established that it should be feasible for hospitals to determine by two or three simple questions and answers whether or not a patient was entitled to free treatment. Mr Jenkin expects the new charges to bring in about £5m a year.

More money promised for the NHS

The Government published its White Paper on public expenditure for the period up to 1983-4 (Cmnd 8175) on 10 March. Expenditure plans for the NHS in the financial year 1981-2 provide for an increase, in real terms, of 1.4% over 1980-1. Nearly 70% of the total NHS spending goes on health authorities' revenue expenditure, which will be about 1.25% higher in 1981-2. Growth in 1982-3 is planned

at 1.7% but final decisions have not yet been taken on the level of spending in 1983-4. For the first time the White Paper gives cash plans for the coming year. Cash spending on the NHS in England will be about £11.1 billion in 1981-2. The cash provided for the NHS in 1981-2 will be over £1000m more than in 1980-1 and about £3500m more than in 1979-80.

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proofed benefits is indeterminate. Though the Government is committed to increasing pensions in line with inflation, any actuarial assessment of index-linked schemes must assume that special measures would be introduced if extreme rates of inflation prevailed over a long period.

The most important contribution of the Scott Report is its support for the principle of maintaining the real income of pensioners—"It is a highly desirable social objective that the standard of living of those in retirement should be protected." The report shows that this principle is clearly recognised in other European countries, like France and West Germany, where pensions are superior to our own and the benefits of index linking are extended to the public and private sectors.

When the Scott Committee was appointed it looked as though index linking was seriously at risk. Successive governments have been unhappy about the costs of inflation proofing, ever since the commitment was first undertaken in 1972. Ironically, the commitment was entered into at a time when inflation rates were still low and when the high rates that have prevailed since were not even contemplated. Indeed, the trade unions negotiating these inflation-proofing arrangements pressed strongly for the link to be made with movements in earnings rather than prices on the grounds that this would be a more equitable basis for calculating increases. But this was resisted by the Government because of the likely cost; it was assumed that earnings would rise more than prices. It is this erroneous assumption that has caused many of the subsequent difficulties. If an earnings link had been established state sector pensioners would not seem to have unfairly benefited by high-price inflation during a period when other incomes were being held down by successive incomes policies.

The membership of the committee was heavily weighted

towards the private sector, in particular banking and finance. Its appointment was viewed with concern by public sector staff and their unions, who assumed that it would arrive at answers favoured by the Government so that the index-linking commitment could then be abrogated. The Scott Committee must be praised for providing an objective report that directs more criticism towards the weakness of private sector pension arrangements than existing public sector index linking.

The report concluded that the comparability exercises undertaken by the review bodies (both the Doctors' and Dentists' Review Body and the Top Salaries Review Body) and in other negotiating procedures (such as Civil Service pay research) provide an acceptable basis for assessing the value of pensions. But, in underwriting these comparability exercises, the committee also recommended that each area of the public sector, including the DDRB, should take full account of their findings when settling remuneration.

Finally, there is a most important but hardly noticed proposal in the Government's recent budget to issue £1000m worth of inflation-linked Treasury bonds for the use of the private sector pension funds. This decision is thought to be unprecedented among Western governments, and the Government should be heartily congratulated on its fast response to this recommendation of the Scott Report. It seems to imply that there is now a firm commitment to retaining index linking in the public sector.

Reference

- ¹ Inquiry into the Value of Pensions. Report. Cmnd 8147. London: HMSO, 1981.