TRANSACTIONS OF SOCIETY OF ACTUARIES
1962 VOL. 14 PT 2

PANEL DISCUSSION

SOCIAL INSURANCE

Panel Members:

FRANK M. REDINGTON, Past President, Institute of Actuaries
REINHARD A. HOHAUS
WILLIAM M. ANDERSON

GREAT BRITAIN

FRANK M. REDINGTON:

All figures have been translated into United States dollars and cents, but, to receive the right impression, they should be roughly doubled because the cost of living for the basic elements of subsistence in Britain is about one-half of that in North America. All social security benefits and contributions in Britain are measured in terms of weekly payments and that must be understood throughout.

HISTORY PRIOR TO 1944

An understanding of our position would be incomplete without a brief historical review. The main developments have been as follows.

Until the opening years of this century, provision for old age was regarded primarily as a matter for the individual and his relatives, but the Poor Relief Act of 1601 placed an ultimate responsibility upon the local community—the parish—and so it remained for three hundred years. Although the relief available under the Poor Law included both cash and kind, any relief given was subject to a searching test of means (including possible support from relatives) and loss of social and some legal status.

Some statutory protection for employed persons who were injured at their work was introduced in the late nineteenth century, but the first acceptance of the general conception of national responsibility came in 1908 with the first Old Age Pensions Act, which gave small noncontributory pensions to persons over 70 subject to a test of means.

The year 1911 was a landmark. The National Insurance Act introduced a contributory scheme of cash benefits during sickness and unemployment and a measure of medical benefits. The scheme was compulsory, although it was limited to employed persons in manual work or in the lower earnings groups. An interesting feature was that the sickness insurance was administered, not by the state, but by private "approved societies" set up by friendly societies, industrial assurance companies, etc., and this system continued until 1948.

The first contributory pensions scheme in the modern sense was introduced in 1925, again for employed persons in the manual or lower earnings groups. It provided old age pensions from age 65 and pensions to widows and orphans and was not subject to a means test. The scheme was not funded. Broadly, employer and employee together paid contributions which were actuarially correct for entrants at age 16, and the Exchequer paid the balance, which, once the transitional period was over, would have been the equivalent of the interest on the nonexisting fund.

Between 1925 and 1945 there were many extensions of benefits and classes of persons covered, but all within the previous general framework. By 1940 Britain's schemes were in many ways very advanced, but they were not well integrated. They were complex, and administration was in the hands of a number of government departments. In the years 1944–48 there was a series of major revisions, most of which came into force in 1948 and form the foundation of our present comprehensive system.

THE REVISIONS OF 1944–48

Previously the national insurance scheme had provided a measure of medical benefits, and also there was overlapping between insurance as of right and assistance under test of means. In 1944–48 the whole area of social security was divided into three: (*a*) the Ministry of Pensions and National Insurance; (*b*) the National Health Service; and (*c*) the National Assistance Board.

The last two are not the subject of today's discussion, but some comments are relevant. The National Health Service was a major new development in 1946. It provides full medical and hospitalization services for everybody in the country. The bulk of the cost is borne by general taxation, but a contribution toward the scheme is included in the weekly amount collected under the National Insurance Act (38 cents from employee and 9 cents from employer). There was some abuse in the early years, which has now been largely removed by making patients pay for a small part of the cost of medicines, spectacles, etc.

National Assistance sweeps into one comprehensive scheme all the arrangements for assistance to persons in real need who for various reasons are not qualified for benefit under National Insurance or for whom benefits are insufficient. Cash benefits do not usually differ much from those available under National Insurance, but help is given toward such things as rent, and extra assistance may be given for dependents.

Our main concern is with those forms of benefit which come under the

Ministry of Pensions and National Insurance. These fall under three main headings.

Family allowances.—A major innovation in 1945 was a weekly cash allowance for each child in a family after the first. The cost is met entirely out of general taxation. The present benefit is about $1.12 a week for the second child, and $1.40 for subsequent children.

Industrial injuries.—Prior to 1946 various Workmen's Compensation Acts provided for compensation from employers to persons involved in accidents or contracting industrial disease at their work. Employers often covered their liability by private insurance, and in some industries (e.g., coal-mining) insurance was compulsory.

In 1946 a comprehensive scheme of compulsory state insurance was introduced to supersede all the previous Workmen's Compensation Acts. Benefits are payable for injury, disablement, and death and are at a considerably higher level than under the main National Insurance scheme. Contributions are shared roughly equally between employer and employee, with a small contribution from the Exchequer (i.e., from general taxation). Exceptionally to all the other plans in Britain, this industrial injuries scheme is funded.

Main scheme.—The main scheme, which came into force in 1948, provides pensions on retirement, weekly benefits for sickness or unemployment, weekly allowances for widows and guardians, maternity benefits, and a small death benefit. With a few minor exceptions, the scheme is universal, although certain classes of contributors are excluded from certain benefits; for example, self-employed persons do not contribute toward, or receive, unemployment benefit. Married women are mostly covered by their husbands' insurance, but, if they are employed, they have the option to be insured in their own right.

The present rates of the main benefits—retirement and widow's pensions, sickness and unemployment benefits—are about $8.00 a week for a single person and $13.00 a week for a married couple. Contributions for employed male persons were roughly $1.00 a week each from the employer and employee for these benefits prior to the revision of the scheme in 1959. The Exchequer supplements these by regular contributions of about one-quarter of the combined amount and, of course, meets any deficiencies.

A word is necessary about the basis of these contributions. The 1948 scheme maintained the so-called insurance principle of previous schemes. The regular contributions from employee, employer, and Exchequer were together equal to the true actuarial funded contribution at age 16, the idea being that throughout an individual's life his benefits would have been properly paid for and were his "by right." The idea was a fiction because there was no fund (other than a small relic of earlier plans) and because the schemes were continually changed, and full benefits were granted to people of all ages (though perhaps with certain transitional qualifications).

The regular contributions were therefore not adequate to provide the benefits, and it was planned that the balance of cost was to be met by the Exchequer. This balance was broadly the interest on the nonexisting fund plus the "back-service" costs of granting increases in benefits and admitting new categories of members at ages over 16.

This was all foreseen in 1948, but inflation overtook the original plans, and, by 1957, the demands on the Exchequer had grown to a politically disturbing figure, and the government actuary was forecasting still further increases until 1980.

RECENT DEVELOPMENTS

This brings me to recent events, which, although still within the category of history, may be of more detailed interest. The account I have given may sound like a beneficent Father Christmas giving presents to all, but to get a true impression it must be remembered that the level of benefits was—and still is—low and that all benefits and contributions were uniform irrespective of the level of the individual's earnings. The principle of the whole scheme was by compulsory state insurance to cover the whole population against every calamity, but at the level of basic subsistence only. Anything beyond that was the responsibility of the individual.

In 1957 the Labour party produced a plan for a radical revision of the pension arrangements. The basic flat pension was to be increased, but, in addition, differential pensions were to be given dependent on previous earnings. Moreover, pensions were to be escalated to meet rising costs and standards of living. The slogan was, "Half-pay pensions for all"—the qualifying clause "in 45 years' time" never seemed to make the headlines. In fact, for the lower-paid workers the pension would ultimately have reached three-quarters of pay, but for the higher paid it would only have been one-third. Contributions were to be a percentage of earnings—5 per cent for the employer, 3 per cent from the employee, and 2 per cent from the Exchequer—and these were for pensions alone. This would have produced an enormous state fund, although still somewhat inadequate by private standards of funding. The booklet said that contracting-out by private schemes would be allowed, subject to various paternal conditions. But how it would be worked has been kept a carefully guarded secret, if indeed it was ever thought about.

The reasons given for this scheme were twofold. The nation was divided into two camps: those with employer pensions and those without. But this, the Labour party claimed, was wrong: pensions should not be largesse from a generous employer; they were a basic right which should be available to all. The other reason was financial. The rising cost to the Exchequer was disturbing; but, as rising inflation led to rising levels of pension benefit, it became politically more difficult to raise the contribution for the lowest-paid workers to adhere even to the principle of the actuarial contribution at age 16.

THE 1959 ACT

The Labour party have not had a chance to put their scheme into operation, although they endorse it at every annual conference.

Perhaps because of the political appeal of the Labour scheme, but partly motivated by the same reasons, the Conservative government introduced a new act in 1959, operative in April, 1961, with three objectives: (1) to place the National Insurance scheme on a sound financial basis; (2) to give a measure of wage-related pensions to those not covered by occupational (i.e., private) schemes; and (3) to encourage the development of private schemes.

The act was a radical departure in principle from the previous arrangements. The scheme is frankly "pay-as-you-go," as, indeed was the previous scheme, but even the flimsy defense of the so-called "actuarial" contribution at age 16 is abandoned—with the approval of most actuaries who dislike the misuse of their adjective in an irrelevant cause. Instead of contributions being uniform, they are graduated according to earnings. As originally planned in 1959, there was to be a *reduction* at lower earnings and an increase at the higher earnings, but the basic benefits and all contributions were increased when the scheme was implemented in April, 1961. The net effect was that the contribution for earnings of $25 a week or less remained unchanged, and, in addition, graduated contributions are payable of 8½ per cent (4¼ per cent each) on earnings between $25 and $42 a week. (To put these figures in perspective, the average weekly wage of industrial workers was about $34 in 1959 and is about $45 now.)

These graduated contributions bring entitlement to a graduated pension on retirement at age 65 at the annual rate of about 1/140th of all earnings in the wage band $25–$42 throughout service. This is very small. The maximum graduated pension to which we can look forward in the year 2010 is about $5.50 a week in addition to the uniform basic pension, which is now $13.00 a week for a married couple and will probably be much larger by 2010. The point should be noted that the graduated contributions are much larger than a private scheme would charge for the graduated benefits except at the old ages. They contain a substantial measure of subsidy from the higher paid to the lower paid and from the young to the old. But arguments based on actuarial justice are hard to substantiate for a "pay-as-you-go" state scheme. Future generations who will foot the bill are not here to join in the debate.

Cynical language could be used about the government scheme. It could be said that it was a device to get more contributions now in return for a promise of wage-related pensions—a promise which is left to the future to redeem. But this can be said in its favor: it has stopped the rapidly rising drain on general taxation and has placed the main burden on the weekly contributions.

Whether it has breached the principle that the state should take care of basic needs and leave the rest to the private sector is a matter of debate. The graduated benefit is so small that it could still be argued that it did no more than recognize that basic needs are not strictly uniform.

CONTRACTING-OUT

One of the most interesting features of the new act is that it allows contracting-out of the graduated benefits—but not the basic. The weekly contribution for contracted-in males ranges from a minimum of $1.02 to a maximum of $1.73. The contribution for contracted-out males is a flat $1.24. The reason for this is that the $1.73 figure contains a large measure of subsidy for the $1.02 figure. Contractors-out could not be allowed to join the subsidized and would not join the subsidizers. On average, $1.24 is near the middle and was (at the time of the passing of the act in 1959) the old rate of contribution which gave the figure a reasonable justification.

The main features of contracting-out are:

a) The scheme must not be opposed by employees, although the decision lies with the employer.

b) The scheme must be approved by the Registrar of Nonparticipating Employments.

c) The scheme must guarantee to every employee, whatever his actual earnings, the maximum state-graduated pension payable not later than 65 (60 for women).

d) On leaving service, an employee must be given either a paid-up deferred pension, or the employer must make a "payment-in-lieu" to the state equal to the arrears of contribution without interest.

e) The scheme must be solvent, but this potentially difficult problem has been treated very lightly. Insured schemes are assumed to be solvent, provided premiums are paid, and self-administered schemes have to submit their accounts supported by an actuarial opinion of solvency up to the level of the maximum state benefits.

The scheme is full of theoretical faults, but it has been a success mainly, it can be argued, because it is so small that the financial balances have taken a secondary place to other considerations. A further vital point is that, because the scheme is so small, it does not appear to be directly vulnerable to inflation. If costs of living rise, the state will undoubtedly increase the rates of pension, but for very many years it will suffice to increase the *basic* pensions only; the graduated pensions will be a trivial element.

The upshot, in spite of many fierce arguments, is that the scheme is working and that over four million persons are contracted-out—roughly one and a half million in the public services, one million in nationalized industries, and one and three-quarters million in private schemes.

THE FUTURE

The future is as fascinating as is any strange and misty landscape. The government scheme has broken some of the ice and eased the way for any Labour scheme. It may be doubted whether the plea that the state should take care of basic needs and nothing more will continue to hold the floor.

It must also be doubted whether the argument about contracting-out is settled. The success of the minute government scheme is not a safe guide to the problem in general, and nobody has yet proposed a satisfactory solution to contracting-out of the Labour scheme unless it is radically altered and, in particular, the escalators against inflation are removed. But the growing practice in private schemes of basing pensions on final salary at date of retirement, which is effectively the same thing, encourages the Labour party in its escalators. The wide spread of private pensions now covering half the population increases the demand that pensions should be regarded as a right and no longer as a luxury.

A further difficulty is that few employers are prepared to grant portable pensions for those who leave their employment. There is no theoretical difficulty in so doing, but the problem of converting employers to this liberal view is formidable. Even more formidable, however, is the administrative problem which would be created if fully portable pensions become general within the private sector.

In most of the Continental countries the state has entered the area of wage-related pensions. The private sector had provided little in the way of pensions, and it appears that the verdict there will be that pensions are a job for the state.