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WEDNESDAY, 10th DECEMBER, 2008

SOCIAL SECURITY DEPARTMENT -
FINANCING OF CONTRIBUTORY SOCIAL
SECURITY SCHEMES

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B I L L E T D'É T A T

TO THE MEMBERS OF THE STATES OF

THE ISLAND OF GUERNSEY

I have the honour to inform you that a Meeting of the States of Deliberation will be held at **THE ROYAL COURT HOUSE, on WEDNESDAY,** the **10th DECEMBER, 2008,** immediately after the meeting of the States of Election already convened for that day, to consider the item contained in this Billet d'État which has been submitted for debate.

G. R. ROWLAND
Bailiff and Presiding Officer

The Royal Court House
Guernsey
14 November 2008

SOCIAL SECURITY DEPARTMENT

FINANCING OF CONTRIBUTORY SOCIAL SECURITY SCHEMES

The Chief Minister
Policy Council
Sir Charles Frossard House
La Charroterie
St Peter Port

26th September 2008

Dear Sir

Executive summary

1. This report, which is intended as a consultation document, examines the options for ensuring the long-term sustainability of the contributory social security schemes, namely the Guernsey Insurance Fund, the Guernsey Health Service Fund and the Long-term Care Insurance Fund. All of those Funds will come under strain from the changing demographic profile of Guernsey and Alderney as the population ages and the ratio of workers to pensioners significantly weakens.

2. The main issue which gave rise to this report was the future role of the States Grants from General Revenue to the Guernsey Insurance Fund and the Guernsey Health Service Fund. The current formula-led nature of those grants, whereby they are linked proportionally to contributions received from contributors and employers was called into question as it conflicted with the policy of the States to confine annual increases in public expenditure within RPI. The position has subsequently changed, through States approval of the 2008 budget (Billet d'Etat XXIII of 2007) whereby formula-led expenditure is not subject to the RPI constraint. Notwithstanding that change, it remains essential to discuss and resolve the financing issues for the contributory schemes.

3. This report contains the historical background to state pensions in Guernsey and their methods of funding, before looking forward with 60 year projections of how the contributory funds would fare under a range of different conditions. The financial modelling is focussed on the Guernsey Insurance Fund, as that fund is by far the largest of the three funds in terms of the contribution rates, the level of the States grant from general revenue and the investment reserves. The Department considers that the preferred future financing structure for the Guernsey Insurance Fund, which will emerge following this consultation process, can be applied very similarly to the two smaller funds.

4. The Department is confident that this report will generate interest and opinion on what should be the preferred blend of options for the sustainability of the contributory funds. Taking into account the views that are expressed by the States when debating this report and the views of the people of Guernsey and Alderney, which the Department will invite from other channels of consultation, the Department will report back to the States in 2009 with firm proposals for the funds.

REPORT

Background

5. On 28 September 2007, having considered a report dated 27 July 2007 from the Social Security Department concerning contribution and benefit rates from 2008 (Billet d'Etat XX of 2007) and with an amendment placed by Deputy Daniel Le Cheminant being carried, the States resolved among other things:

'That the Social Security Department should carry out a comprehensive review of the long-term future funding of the Guernsey Insurance Fund, Guernsey Health Service Fund and the Long-term Care Insurance Fund in conjunction with the Treasury and Resources Department, and that -

(a) the Review should, in particular, encompass all possible options for contribution rates, the level of the States Grant and the retirement age and include actuarial advice and wide consultation, and

(b) the results of the Review should be reported to the States as part of the Benefit and Contribution Rates Report in September 2008'.

6. On 25 June 2008, the Minister of the Social Security Department made a statement to the Assembly, informing the members that, while substantial progress had been made with the financial modelling, including the actuarial projections, the progress had not been such as to enable the Department to report as required at the September 2008 States meeting. The Minister said that, in particular, there had been no consultation with the community on the merits of increasing retirement age. The Minister said that Department was preparing a report for the December 2008 States meeting, which would be in the form of a consultation document allowing a full exploration of the funding issues relevant to the sustainability of the contributory social insurance schemes.

7. This report forms the consultation document referred to in the Minister's statement of 25 June 2008. The Department anticipates that, following the December consultation report and the investigation of ideas that flow from that process, the Department will be in a position to return to the States in May or June 2009 with firm proposals for the level of the States grants, contribution rates and upper earnings limits to apply in 2010 and beyond. The report will also contain a recommendation regarding future pension age.

The three contributory funds

8. The Social Security Department is responsible, by Law, for the control and management of:

    1. The Guernsey Insurance Fund
    2. The Guernsey Health Service Fund
    3. The Long-term Care Insurance Fund.

9. The Guernsey Insurance Fund provides a broad social security coverage against contingencies that may interrupt or end wage earning capacity. These contingencies include sickness, unemployment, work-injury and old age. The Guernsey Insurance Fund has an annual turnover of approximately £93m in 2008 terms. Of the benefits provided, old age pension is by far the most expensive for the Fund, accounting for £66.6m of expenditure in 2007, followed at a distance by invalidity benefit at £5.5m, sickness benefit at £2.8m and bereavement benefits at £2.1m. The Fund has investment reserves of approximately £500m.

10. The Guernsey Health Service Fund provides the pharmaceutical service, through which Guernsey and Alderney residents receive prescription drugs for a nominal charge, or free of charge in the case of pensioners. The Fund also pays for the specialist health insurance scheme, which covers out-patient and in-patient treatment by the Medical Specialist Group and the Guernsey Physiotherapy Group. The Fund also pays for medical consultation grants which subsidise the cost of a consultation with a General Practitioner or nurse by £12 and £6 respectively. The Guernsey Health Service Fund has an annual turnover of approximately £36m. The Fund has investment reserves of approximately £49m.

11. The Long-term Care Insurance Fund provides financial assistance with the cost of fees for residential and nursing homes. The Long-term Care Insurance Fund has an annual turnover of approximately £16m. The Fund has investment reserves of approximately £20m.

12. It can be seen that all three funds are holding substantial investment reserves which are far in excess of what would currently be needed for pure pay-as-you-go social security schemes. But those reserves will soon be called upon to moderate the financial impact on the funds of the changes in the demography of Guernsey and Alderney. The well documented ageing of the population and the substantial increased numbers of elderly residents relative to those of working age is a process that is underway and accelerating.

13. If there were no reserves in the contributory funds, contribution rates would have to increase substantially over time in order for broadly the same numbers of people of working age to pay the benefits for a doubling of the number of pensioners. That stark situation can be eased by using first the investment income of the funds and subsequently drawing down on the capital value of the funds in order to maintain contribution rates at reasonable levels.

History of contributory old age pension scheme

14. The history of Guernsey's state pension warrants more than just an overview, as it contains interesting facts on financing, coverage, pension age and retirement age, all of will inform and assist consideration of the current issues.

15. Old age pensions started in Guernsey on 1 July 1926, with the coming into force of the Old Age Pensions Law 1926. Pension age was 70, at a time when the period life expectancy at birth in England and Wales, was 58 for men and 62 for women. The scheme was non-contributory, with all funding coming from the States. The scheme was means tested and the maximum pension was 8 shillings (40p) per week, payable to a person with income of less than £38 per year. The pension reduced in increments of 1 shilling as income rose, with a minimum pension of 1 shilling (5p) per week payable to a person with income of up to £52 per year. No pension was paid if income exceeded £52 per year.

16. The non-contributory scheme, while being a groundbreaking social policy for Guernsey, was only partially successful. By as early as 1928, the law was being amended in order to make the conditions of entitlement more stringent, and by 1932 a second set of revisions were so extensive as to justify the 1926 Law being entirely repealed and replaced by the Old Age Pensions Law 1931. The non-contributory pension was perceived to be over-generous and to being exploited by 'opportunists'. Included in the 1931 Law was a disqualification from pension for *'a person who has habitually failed to work according to his ability, opportunity and need.'*

17. As reported to the States by Mr Edward T Wheadon, President of the States Insurance Authority and Mr Thomas E Ozanne, President of the Old Age Pensions Authority in a letter dated 14 July 1931 (Billet d'Etat X):

> *'One of the main objections to the present system is that it penalises thrift; it is in general terms a glorified system of relief and until the amendments adopted have the force of law, it is not always necessitous relief.'*

18. The above letter went on to explain to the States that the principal barrier to having a contributory pension scheme, when the non-contributory system was being designed in 1924, was that there appeared to be no practical machinery for the collection of contributions from individuals. By 1931, that barrier no longer existed because the States Insurance Authority was collecting contributions for the Accident to Workers Law, 1924, which came into effect in 1925. The Old Age Pensions Authority and the States Insurance Authority had agreed that the same system of collection could be used for work-accident insurance, old age pensions and also for widows and orphans benefits which were by then being considered.

19. On 9 June 1933 (Billet d'Etat VI) the Old Age Pension Authority proposed an extension of the accident insurance scheme to include contributory old age pensions, widows benefits and orphans benefits.

First contributory pension

20. The Contributory Pensions Law, 1935 came into force on 1 July 1935, whereupon the States Insurance Authority and the Old Age Pensions Authority merged into the single States Insurance Authority. The Law consolidated the provisions of the Accident to Workers Law and set common rules on insurability. Workers were compulsorily insured if their earnings were less than £3 per week. There was an option to be voluntarily insured for people who had once been compulsorily insured but whose earnings had risen to exceed £3 per week. This option was withdrawn if earnings exceeded £6 per week. Pension age under the Contributory Pensions Law remained at 70, although by that time, the UK had introduced a contributory scheme with a pension age of 65. In 1935 the period life expectancy at birth in England and Wales was 60 for men and 64 for women.

21. The States Insurance Authority reported having to decline a large number of applications for voluntary insurance from people who were earning above the wage limits or were self-employed. In the early days this was seen as an endorsement of the merits of contributory insurance. But with the passage of only a few years, the limited cover of the contributory pension system was showing its deficiencies.

22. In July 1946, the States considered a report from the States Insurance Authority containing proposals for extensive reform of the social insurance system. The origins of that report lay in a visit to London by the President and Administrator of the Authority, just 3 months after the Liberation, when they received a full briefing on the report by Sir William Beveridge which had been presented to the UK Parliament in November 1942. The Beveridge Report, of course, was the foundation for the UK welfare state, including the National Health Service and the National Insurance Acts.

23. Reporting to the States of Guernsey (Billet d'Etat XVIII of 1946), the States Insurance Authority promoted the main strength of the 1935 contributory pensions system as being that *'it provides pensions for old age avoiding all tests other than those of age and a number of contributions'*. The issues of means testing, in particular the situation where a benevolent employer may have made some provision or financial gift for an employee's retirement, with the unexpected consequence of denying the individual a means-tested non-contributory pension, had caused much dissatisfaction with the 1926 non-contributory pension system.

24. But the main deficiency in the 1935 contributory pension scheme concerned its limited coverage, as it insured only low income workers employed under a contract of service. The self-employed were excluded. The 1946 report to the States observed that *'many persons working on their own account are poorer and more in need than many employees'*. The effect of the war years was also very relevant and the report commented that *'Many would not be in need but for circumstances entirely beyond their control arising out of the war and the German occupation.'*

Proposed 'National Insurance' for Guernsey - then annulled

25. On 26 November 1947 (Billet d'Etat XXIX) the States Insurance Authority proposed to the States a system of compulsory social insurance, to cover all employed, self-employed and non-employed people, closely modelled on the National Insurance Act. In line with the UK provisions, it was proposed that pension age should reduce from 70 to 65 for men and from 70 to 60 for women. The proposal was for a retirement pension, not an age pension, meaning that pension would not be payable until the individual had substantially stopped work. Pension would be paid at the age of 70 whether or not the individual continued to work. The States approved the proposals and the preparation of legislation.

26. The Projet de Loi for the comprehensive new scheme was approved by the States and subsequently received Royal Assent. However, growing opposition had attended the passage of the legislation and when the Appointed Day Order was laid before the States in February 1952 it was annulled. This meant that state pension provision continued under the inadequate Contributory Pensions Law, 1935 and pension age remained at 70 for men and women.

27. In May 1963 (Billet d'Etat VII) the States Insurance Authority returned to the States with renewed proposals for a comprehensive system of social insurance, including a proposed reduction in the pension age for women, from 70 down to 65, leaving pension age for men at 70. The States resolved that the Authority should report back on a scheme which had either a common retirement age of 65 for both men and women or different retirement ages of 65 for men and 60 for women.

First comprehensive social insurance scheme

28. The States Insurance Authority reported back in February 1964 (Billet d'Etat III) proposing a system including retirement pensions at age 65 for men and women. This was approved by the States, together with other proposals which justified the preparation of a new law.

29. The Social Insurance (Guernsey) Law, 1964, came into effect from 4 January 1965. Pensionable age under the 1964 Law was 65 for men and women. In 1965 the period life-expectancy at birth in England and Wales was 69 for men and 75 for women.

30. The new pension was a retirement pension. If an individual continued to work after reaching 65, and had earnings exceeding £4 10s (£4.50) per week, the retirement pension was reduced by sixpence (2.5 pence) for every shilling (5 pence) earned up to earnings of £5 10s (£5.50) per week after which the pension was reduced by a shilling for every shilling earned. Pension was paid at age 70, without any reductions in respect of earnings, whether the individual continued to work or not. Where a person was prevented by the earnings rule from receiving any pension at all, the amount of the pension eventually received on retirement, or at age 70, was increased by increments. When the 1964 Law

came into operation, it provided for an incremental cash addition to the eventual weekly pension for each 10 additional contributions paid. This was later amended to an increment for every additional 9 contributions paid.

31. In February 1970, the States Insurance Authority reported to the States with proposed revisions of the pension scheme. By that time, 'the earnings rule' had become widely unpopular. The States decided to maintain a retirement pension, but to abolish the earnings rule. The pension would be paid at age 65 unless the individual opted to continue paying insurance. The size of the increments for pensions paid later than 65 would be increased.

32. The above Resolutions of the States did not form a cohesive structure and the Authority returned to the States in May 1970 (Billet d'Etat XI). The States resolved to delete all references to retirement pensions and to replace with the name 'old age pension' but with the right to defer receipt of the pension until the age of 70.

The earnings-related social security scheme

33. In September 1976 (Billet d'Etat XV), the Authority reported to the States with proposals to change social insurance contributions from flat-rate stamps to earnings-related contributions. In that report, the Authority explained that there was minimal take-up of the option to defer receipt of old age pension. Indeed in 1975 there had only been 1 request to defer the pension. The States resolved that the option to defer pension be removed from the new social insurance legislation. Accordingly, when the Social Insurance (Guernsey) Law, 1978 came into force on 1 January 1979, the option to defer old age pension had been removed. Pension age remained at 65 for both men and women. In 1979, the period life-expectancy in England and Wales was 70 for men and 76 for women.

34. The poor take-up of the right to defer pension is rather surprising, as the increments were, at the time, generous. In 1975, when the full pension was £12 per week, the increments for deferral were 30p for every 9 weeks of deferral. This meant that deferring for the full 5 years until the age of 70 would increase the £12 pension to £20.70 per week.

35. A small number of people are still receiving increments to their pension in respect of contributions paid by themselves or their spouse under the 1964 Law. But the current value of those increments is now minimal because, once awarded, their value was never increased through the general increase in benefits or any other form of indexing. Although this may now appear very strange, it should be noted that throughout the life of the Contributory Pensions Law, 1935 and its successor, the Social Insurance (Guernsey) Law 1964, prices barely moved. It was not until the early 1970s, when repeal of the increments system was underway, that high rates of inflation began to be experienced and necessitated regular uprating of the benefits.

36. The 1978 Social Insurance Law, as amended, remains the principal legislation under which the current social insurance scheme, including old age pension is

administered. In 2008, the estimated period life-expectancy in England and Wales is 78 for men and 82 for women. Life expectancy in Guernsey is higher than in the UK. It was reported in the 109th report of Guernsey's Medical Officer of Health that life expectancy for men and women at age 60 in Guernsey was 23 years, which is nearly 2 years more than the UK.

History of States grants to the social insurance schemes

37. The 1926 Non-contributory Pensions Law was 100% financed from general revenues of the States.

38. The Contributory Pensions Law, 1935 was financed approximately 50% from general revenues of the States and 50% from employees and employers.

39. The Social Insurance (Guernsey) Law, 1964 was financed approximately 40% from general revenues of the States and 60% from contributors, namely employees, employers, self-employed and non-employed.

40. The Social Insurance (Guernsey) Law, 1978 commenced with financing of 36% from general revenue and 64% from contributors. The financing from general revenue has, to date, been by way of a percentage of contribution income received by the Guernsey Insurance Fund. For illustration, the 'States Grant' from 1979 to 2003 was equal to 57% of contribution receipts. For every £1 of contributions collected, the States Grant would be 57p. This meant that as a proportion of total income to the Fund, excluding investment income, the States Grant was 36% (57p divided by 157p = 36%).

41. The States Grant was reduced from 57% to 50% from 1 January 2004 in accordance with actuarial advice. It was further reduced to 36% from 1 January 2007 and to 15% from 1 January 2008 in accordance with the Resolutions of the States concerning the Future Taxation and Economic Strategy (Billet d'Etat XI of 2006).

42. The movement in the percentages of the States Grant and the proportion of income to the Guernsey Insurance Fund that the grant represents, are summarised in the table below.

States Grants to Guernsey Insurance Fund		
	Percentage of contribution income	Proportion of income to Fund*
1 January 1978	57%	36%
1 January 2004	50%	33%
1 January 2007	36%	26%
1 January 2008	15%	13%

* excluding investment income

43. The States Grant to the Guernsey Insurance Fund amounted to £23.47m in 2007 and is expected to be £12.20m in 2008.

States Grants to other contributory social security funds

44. A States Grant is also made to the Guernsey Health Service Fund. The grant is currently 12% of contribution income to that Fund. The movement in the grant is summarised below.

States Grants to Guernsey Health Service Fund		
	Percentage of contribution income	Proportion of income to Fund*
1 January 1991	57%	36%
1 January 1996	36%	26%
1 January 2003	40%	29%
1 January 2007	27%	21%
1 January 2008	12%	11%

* excluding investment income

45. The States Grant to the Guernsey Health Service Fund was £7.30m in 2007 and is expected to be £3.9m in 2008.

46. A further States Grant, payable to the Long-term Care Insurance Fund, ceased entirely from 1 January 2007.

Options for future level of States Grant

47. In the letter of comment appended to the Social Security Department's proposals for benefit and contribution rates for 2008 (Billet d'Etat XX of 2007) the Minister of the Treasury and Resources Department wrote:

> *'The continued application of the **current** method of calculating the States grants will result in short-term above RPI increases in the grants, at a time when the States has agreed that increases in public sector expenditure should be restrained to RPI or less. This will then be followed by progressive, real term decreases in the level of the grants to the social security funds from General Revenue, leading to the eventual end of the requirement for these States Grants.*
>
> *The Treasury and Resources Department therefore believes that it is essential that a review of the method of calculating the States grants is carried out jointly with the Social Security Department.'*

48. In the same Billet d'Etat, the above comments were strongly endorsed by the Policy Council, which gave notice of its intention to place an amendment seeking to defer a decision concerning the States Grants until the Budget Report of that year. An amendment to that effect was in due course placed, but not carried by the States. Instead, the States approved an alternative amendment, the wording of which appears at paragraph 5 of this report and which required the preparation of this report.

49. The Department understands the Treasury and Resources Department's wish for certainty over as much as possible of its expenditure from General Revenue, particularly where the items of expenditure are large, as is the case with the grants to the contributory funds.

50. The Department has strongly advocated maintaining the formula-led States Grant, seeing it as a strength of the system, not a weakness, that the amount of the grants may increase substantially if contribution receipts happen to rise. The Department's support has been based on the logic that if contribution receipts have risen, then almost certainly income tax ETI returns will also have risen and the increased grants should be affordable to the Treasury. Conversely, when the economy is performing less well, and contribution receipts are lower, then so will the States grant be lower.

51. Having repeated that line of argument, the Department acknowledges the substantial changes that have occurred in the financing of the contributory schemes since the States determined its Future Economic and Taxation Strategy in June 2006. The Department acknowledges that 'the insurance principle' on which the pricing of contributions for the social insurance and other contributory schemes was based has been eroded. This requires the financing of the schemes to be viewed afresh.

52. The insurance principle that applied until 2007 was a very simple concept. Recognising the pay-as-you-go nature of the scheme, the price of the social insurance premium was calculated by dividing annual benefit and administration expenditure by the number of contributors. The resultant premium, which in 2006 was approximately £50 per week for Guernsey Insurance Fund benefits alone, was then arrived at through applying a percentage contribution rate against an upper earnings limit. People with earnings at or above the then upper earnings limit of £36,036 per annum would, with their employer, be paying 7.3% of £36,036, amounting, to £2,631 per year, or £50 per week. People earning less than £36,036 per year in 2006 would be paying lower contributions. For example, a person earning £20,000 per year would, with his employer, be paying £1,460 per year (7.3% of £20,000) or £28 per week. The shortfall in the £50 true premium and the £28 paid was made good by the States Grant from General Revenue.

53. Through States approval and implementation of the Economic and Taxation strategy, a person paying contributions at the 2008 upper earnings limit of £64,896 per year is now paying substantially more than the pay-as-you-go premium for the social insurance scheme and, for that matter, for the Health Service and Long-term Care schemes as well. Employers, who for high earners are paying contributions on earnings up to £108,108 per year are paying even higher premiums. These measures, and the compensatory reductions in the States grants, have reduced the draw on general revenue by more than £26m per year in 2008 terms.

54. In the new arrangements, the social security contributions paid to the contributory schemes by high earners and their employers take the form of a

hypothecated social security tax. This is because the contributions, while being at a much higher for some, are used only to pay social security benefits and do not enter general revenue to meet other governmental expenditure obligations.

55. Over the last 2 years, as described, substantial changes to the financing of the contributory schemes have taken place. Although the Department resisted those changes when proposed, it now is keen to look forward not back.

56. The main options regarding the States grants from General Revenue are:

   1. continuation with a formula-led grant at the current percentage of contribution income or a higher or lower percentage; or

   2. conversion to a cash amount for the grant and index annually by RPI or some variation of RPI; or

   3. conversion to a cash amount for the grant, to continue at that nominal level without indexing.

57. Charts showing the impact of these different scenarios on the sustainability of the Guernsey Insurance Fund follow later in this report at paragraphs 107 to 150.

Options for contribution rates and upper earnings limits

58. Social Security contributions are collected for the Guernsey Insurance Fund, the Guernsey Health Service Fund and the Long-term Care Insurance Fund. The contribution rates for the 3 funds, shown in their component parts and combined, are as follows:

2008 contribution rates

Employed persons		
Employee		
Social insurance	3.2%	
Health insurance	1.4%	
Long-term care	1.4%	
		6.0%
Employer		
Social insurance	4.9%	
Health insurance	1.6%	
Long-term care	0.0%	
		6.5%
Total		12.5%

Self-employed persons		
Social insurance	6.3%	
Health insurance	2.8%	
Long-term care	1.4%	
		10.5%

Non-employed persons under 65		
Social insurance	5.7%	
Health insurance	2.8%	
Long-term care	1.4%	
		9.9%

Non-employed persons over 65		
Social insurance	0.0%	
Health insurance	1.2%	
Long-term care	1.4%	
		2.6%

59. The reason for different percentages for different types of contributor is that there are some variations in the benefits being paid for. For example, the self-employed contribution rate of 10.5% is less than the 12.5% rate for the employed contributor and the employer, because, firstly, the employer is paying an extra 1% as part of the economic and taxation strategy and, secondly, the self-employed contributor is not entitled to unemployment benefit and, therefore, not paying towards it. The non-employed contributor under the age of 65 is paying less than the self-employed person because non-employed persons are not insured for unemployment benefit, or sickness benefit or industrial accidents. The contributor over the age of 65 is no longer paying towards the social insurance benefits of pension, sickness, invalidity and so on.

60. Having explained some of the differences, the principles of which remain valid, the Department is aware that the substantial recent changes in the upper earnings limits have had a distorting effect on the precise allocation of contributions across the three funds and will address that issue as a separate matter. The issue does not affect the headline rates of the combined contributions for all funds, and it is the headline rates that are material to this consultation process on sustainability of the funds.

Upper earnings limits

61. The upper earnings limits for 2008 and 2009 are shown below

	Annual upper earnings/income limits	
	2009	2008
Employed, self-employed and non-employed persons	£69,108	£64,896
Employers	£115,128	£108,108

62. According to the Department's records from contribution returns, in 2006 when the upper earnings limit was £36,036 per year, 23% of employed persons were earning more than that figure.

63. The contribution returns to date for 2008 show that 8% of employed persons have earnings above the upper earnings limit of £64,896 and 3% have earnings above the upper earnings limit of £108,108 which applies to employers.

64. According to the Department's records, 18% of self-employed persons have earnings above the upper earnings limit of £64,896.

65. Some of the options as regards the upper earnings limits (UEL) include:

1. increasing the UEL for contributors to match the higher employer limit;
2. further increasing the UEL for employers and contributors;
3. removing the UEL entirely for employers;
4. removing the UEL entirely for contributors.

66. While the removal of the upper earnings limits may appear an attractive option, and while acknowledging that there is no upper earnings limit for employers in the social security contributions that apply in the UK and the Isle of Man, the Department has reservations. Removing the cap from the employers' side of the contribution would affect the top 3% of earners. Any estimated additional contribution returns from those earners would have to be treated with caution as it could easily be affected by organisational change, or avoidance, leading to diminishing returns from the initiative. As a simple illustration, an organisation employing very high earning staff may choose to have them based in Jersey, where the upper earnings limit is currently £40,728 per annum. Such a relocation would not only lose Guernsey the social security contributions but also the high earning employee's 20% personal income tax returns.

Comparison of contribution rates and upper earnings limits in Guernsey, Jersey, UK and Isle of Man

67. The table below contains a comparison of contribution rates and upper earnings limits in Guernsey, Jersey, the UK and Isle of Man. It should be noted that these headline contribution rates cover different benefits between the territories. For example, Guernsey is the only territory that has a contribution for long-term care.

Table to be read with notes overleaf	**Guernsey** 2008	**Jersey** 2008	**UK** (08/09)	**Isle of Man** (08/09)
Employed persons	**Employer/Employee**	**Employer/Employee**	**Employer/Employee**	**Employer/Employee**
Percentage rate up to upper earnings limit	6.5%/6.0%	6.5%/6.0%	12.8%/11%	12.8%/10%
Percentage rate after upper earnings limit			12.8%/1%	12.8%/0%
Upper Earnings Limit per week	£2,079/£1,248	£783	Unlimited/£770	Unlimited/£695
Lower Earnings Limit per week	£105	£165	£105	£105
Threshold per week			£90	£90
Self-employed				
Percentage rate up to upper earnings limit	10.5%	12.5%	8%	8%
Percentage rate after upper earnings limit			1%	
Annual Earnings Max Min	£64,896 £5,460	See below See below	£40,040 £4,825/£5,435	£36,140 £5,435
UK flat rate payable weekly as well as % rate on earnings			£2.30	£2.30
Non-employed	9.9% 2.6 % (over 65)			
Annual Income Max Min	£64,896 £13,650		Flat rate £8.10 p/w	Flat rate £8.10 p/w

Notes

UK/IOM apply a 1.6% employee's contracted out rebate.

UK/IOM apply a 3.7% employers' contracted out rebate (salary related schemes) and 1.4% (money purchase schemes).

UK/IOM retain a married woman's rate of 4.85% UK and 3.85% IOM

UK/IOM calculate liability after deducting the value of the lower earnings limit from gross earnings (in the UK, for the self employed, the value of the Lower Profit Limit is first deducted - £5,435)

Jersey calculates liability on a monthly basis; figures shown have been converted to weekly values for comparison purposes.

Jersey retains a married woman's option (applies if liable and married before 1 April 2001) where the married woman can choose to pay or not to pay contributions.

Jersey does not distinguish between self-employed and non-employed contributions, which are both based upon income.

Jersey applies an upper limit for self-employed and non-employed of £40,728 on earnings and £54,304 on the total of earnings and unearned income.

Jersey applies a lower limit for self-employed and non-employed of £7,956 of earnings with total income below £27,152 or £13,703 of total income.

Benefit uprating policy

68. On annual recommendations from the Social Security Department, the States have, over time, approved increases in the level of old age pension, and other contributory benefits, which have been ahead of the increase in RPI. While there has no explicit formula for benefit uprating in the legislation, the customary uprating has been at the mid-point of the increase in prices and the increase in earnings. In some years, in particular the 5 year period 2002 to 2006, pensions have been increased above the mid-point. In other years, increases have been closer to RPI.

69. In the UK, since 1979 the basic state pension has been increased annually by RPI only. Prior to 1979 it was increased in line with the increase in earnings. The UK pension, which, is currently £90.70 per week compares poorly against the Guernsey pension of £160.75 per week and serves to illustrate the long-term effects of uprating by prices only. The UK will be restoring the link to uprating pension in line with earnings from 2012, this being one on the key reforms contained in the UK Pensions Act 2007. The reforms of the UK state pension follow the findings of the Pension Commission chaired by Lord Adair Turner, which reported its findings in 2005, and the subsequent white paper 'Security in Retirement' which was published in 2006.

70. If pensions are not increased in line with the increase in earnings, then pensioners do not share the generally increasing prosperity of the community. The buying power of the pension may well keep pace with the items against

which RPI is measured, but the lifestyles and social inclusion of pensioners falls relative to that of the population of working age. There is a further argument for maintaining the contributory state pension at a good rate because the higher the pension the greater the reduction in general revenue financed supplementary benefit top-up payments for pensioners.

71. By way of example, when the Guernsey social insurance scheme switched from flat-rate contribution stamps to earnings related contributions, in 1979, full rate old age pension was £20 per week. Had that pension been increased by Guernsey RPI, its rate in 2008 would have been £90.71, which would surely be considered grossly inadequate. Instead, through the policy of uprating ahead of RPI, full rate Guernsey pension in 2008 is £160.75 per week.

72. However, although Guernsey can take some satisfaction from the extent to which its basic state pension has exceeded the increase in RPI over time, this should be balanced by acknowledgement that the uprating policy is one that knowingly falls short of the increase in earnings. In the same way that the current level of the UK basic state pension demonstrates the inadequacy of the UK benefit uprating policy, so will the 'half-way house' uprating policy for the Guernsey pension be proven inadequate, albeit on a much longer timescale. It should be noted that, since 1998, Jersey old age pensions have been uprated in line with earnings.

Second pillar pensions

73. In drawing attention to the substantial difference between the level of basic state pensions in Guernsey and in the UK, which are termed 'first pillar' pensions, it should be noted that many UK pensioners will have additional entitlement to second pillar schemes such as the State Earnings Related Pension Scheme (SERPS), State Second Pension, or a Stakeholder pension scheme provided by employers as an alternative to contributing to the state-provided second pillar schemes. The terminology of 'pillars' in retirement provision is in wide international usage and the second pillar is used to describe further compulsory contributions to a pension scheme beyond the basic pension of the country concerned. Contributions to SERPS in the UK system was compulsory, unless the employee was contributing to an approved scheme elsewhere, typically the employer's scheme, in which case a reduction was allowed in the contributions to the UK government scheme. This was the so called 'contracting in' or 'contracting out'. The second pillar schemes do not follow the flat-rate benefit nature of the basic state pension, but instead have benefits that are related to the value of the contributions paid by the individual. 'Third pillar' provision refers to private provision of the individual through voluntary savings and investments beyond the compulsory pension contributions of the first and second pillars.

74. Guernsey does not have a compulsory second pillar pension, although many employees, particularly those in the finance industry, professional services and the public sector will be members of occupational pension schemes.

Pension age in other countries and proposals for change

75. A state pension age of 65 is commonly found throughout Europe and worldwide. Currently, very few countries have a higher pension age, two notable exceptions being Iceland and Norway, where state pension age is 67 for men and women. Many more countries currently have a state pension age that is less than 65, with the age of 60 being commonly found. There is also the opportunity in many countries to take the state pension even earlier at a reduced actuarial value.

76. Whatever the current pension age of the country in question, the policy makers will almost certainly be giving serious consideration as to how that age may be increased in the future. Such consideration is being driven partly by fiscal issues as the expenditure of state pensions increases both through increasing life expectancy and through the increasing size of the cohorts about to reach pension age, particularly from 2010 onwards. There is also the key issue of the relative proportions of the economically active to inactive sectors of the population, in other words the number of workers to pensioners. This is a particularly relevant issue in Guernsey where the island has resolved to keep its population to approximately the same level as in April 2007, that figure being 61,800.

77. Changes to the State pension age properly require long-term planning, notice and implementation. It would probably be unreasonable to give effect to any change in state pension age at less than 10 years notice. This seems to be the approach taken by countries which have announced their intentions to increase the pension age.

United States

78. The United States has already started gradually increasing retirement age. The process stated in 2003 and retirement age has now increased from 65 to 65 and 10 months in 2008. Retirement age will hold at 66 between 2009 and 2021, after which it will gradually increase to 67 by 2027. The US will, however, continue to allow pensions to be paid at 62 years of age at actuarially reduced values.

Denmark

79. In Denmark, State pension age is planned to increase from 65 to 67 over a four year period from 2024 to 2027, inclusive.

United Kingdom

80. State pension age in the UK will increase from 65 to 68 between 2024 and 2046. Although the full changes take place over a 22 year period, or 38 years from the present date, each incremental change occurs over a much shorter, 2 year period, as set out below:

- Pension age 65 until 2024
- Increases to 66 over 2 years between 2024 and 2026
- Pension age 66 from 2026 and holds for 8 years
- Increases to 67 over 2 years between 2034 and 2036

- Pension age 67 from 2036 and holds for 8 years
- Increases to 68 over 2 years between 2044 to 2046
- Pension age 68 from 2046

Germany

81. State pension age in Germany will increase from 65 to 67. The increase from 65 to 66 will take place over 12 years and the increase from 66 to 67 will take place over 6 years as set out below:

    - Pension age 65 until 2012
    - From 2012 pension age increases 1 month per year
    - Pension age 66 in 2023
    - From 2024 pension age increases 2 months per year
    - Pension age 67 in 2029

Increasing pension age to 70

82. Lord Turner, Chairman of the UK Pensions Commission (see para 69.) has been widely quoted as saying that the proposed new UK pension age of 68 is not the end of the story and that pension age would be 70 by the end of the century.

83. In addition to considering the paths being followed by other countries, the Social Security Department has given thought to the implications of increasing pension age to 70 years of age. While that may appear a very big step to take, it must be remembered that a long timescale is envisaged for any substantial increase in pension age. If, following the consultation process, the States were of the view that a long-term pension age of 70 was called for, the Department would promote the approach set out below. This would involve changes beginning to take effect from 2020 and ending in 2050, when pension age would be 70.

84. Under this option, pension age would remain at 65 until 2020. Pension age would then increase by 2 months each year.

85. So in 2021, pension age would be 65 years and 2 months. In 2022 pension age would be 65 and 4 months. In 2023, pension age would be 65 years and 6 months, and so on.

86. Through this approach, the following milestones would be reached:

Year	Pension age
2020	65
2026	66
2032	67
2038	68
2044	69
2050	70

87. To work out how this would impact on an individual's own case, the calculation is:

Pension age = 65 + (Year of 65th birthday - 2020) x 2 months

88. So for, say, a 30 year-old person, who will be 65 in 2043, the calculation is:

Pension age = 65 + (2043 - 2020) x 2 months

= 65 + 46 months

= 68 years and 10 months

89. The first age group which would have a pension age of 70, would be people born in 1985 or later. In other words people currently aged 23 or less would have a pension age of 70.

Demography and pension age

90. According to Social Security Department records, the population of Guernsey and Alderney in March 2007 was 64,071, with the broad divisions of school age, working age and pension age as follows:

March 2007 Population of Guernsey and Alderney	
People aged 0 to 15	10,682
People aged 16 to 64	43,056
People aged 65 and over	10,334
	64,071

91. The figures show that in 2007 there were 4.2 people of working age for every 1 person of pension age resident in Guernsey and Alderney. This is called 'the support ratio'.

92. Assuming that there is no growth in the overall population of Guernsey and Alderney between 2007 and 2060, which is the current States policy on population levels, the age profile within the population is projected to change to that shown below:

2060 Population of Guernsey and Alderney (no growth)	
People aged 0 to 15	8,900
People aged 16 to 64	36,703
People aged 65 and over	18,468
	64,071

93. The 2060 projections are that there will be just under 2 people of working age for every 1 person of pension age resident in Guernsey and Alderney.

94. It should be noted that the context here is of the demography of the resident population. The support ratios of residents over pension age to people of working age are highly relevant to economic issues including the size of the working population necessary to generate wealth and to finance and service the infrastructure and social services, in their widest sense.

95. However, not every resident of working age will be in work and not every resident of pension age will be receiving a pension. On the other hand, many pensions will be paid from the Guernsey Insurance Fund to people who have contributed to Guernsey but now live overseas, just as many pensions will be paid into Guernsey from other countries where Guernsey's residents have formerly worked and contributed. In terms of the financing of the social insurance scheme, the Government Actuary's Department looks at the ratio of the projected number of contributors to the projected number of pensioners. The number of pensioners includes the off-island pensions and, consequently, the ratios are substantially worse than the support ratios shown above. The number of pensions paid off-Island will continue to increase for the period of the projections. Most of those off-island pensions will be part-pensions and in many cases, the pension will be very small, but it is important not to lose sight of this fact.

96. In 2007, Guernsey was paying 14,380 pensions, of which 9,937 were being paid in Guernsey and Alderney and 4,443 elsewhere in the world. In 2007 there were 34,331 contributors. The ratio of contributors to worldwide pensioners was therefore 2.4 to 1.

97. The Government Actuary projections show that in 2060 there will be approximately 23,600 pensioners and 29,900 contributors, meaning that the ratio of resident contributors to worldwide pensioners reduces to just 1.27 to 1, if there is no change to pension age.

98. If the pension age were to increase to 70 by 2050, as is one option identified in this report, it is estimated that in 2060 there would be approximately 19,200 pensioners and 31,600 contributors. This would improve the ratio of resident contributors to worldwide pensioners to 1.65 to 1.

99. Having acknowledged the pensions paid outside Guernsey and Alderney, this report returns to viewing the demography of the resident population.

100. If the pension age were to increase to 70 by 2050 the broad divisions of the population into those of school age, working age and pension age in 2060 would be as overleaf:

2060 Population of Guernsey and Alderney (no growth) Pension age of 70	
People aged 0 to 15	8,900
People aged 16 to 69	40,615
People aged 70 and over	14,556
	64,071

101. Instead of the support ratio of 2, as shown in paragraph 93 above, increasing the pension age from 65 to 70 improves the ratio to 2.8. This substantial improvement comes about from the reduction of 3,912 in the number of people of pension age and the addition of that same number of 3,912 to the number of people of working age.

Modelling the options for change

102. The future sustainability of the contributory social insurance scheme will depend on the interaction of numerous factors, some of which are fully within the control of the States and others which are less controllable or uncontrollable.

103. For example, the States can fully control:

- the contribution rates for individuals and employers
- upper earnings limits for contributions
- benefit rates
- benefit conditions, including pension age
- the amount of the States grant

104. The States can influence, but only partly control:

- the local economy, employment levels and earnings
- the number of workers and, consequently, contributors
- fertility rates

105. The States cannot control:

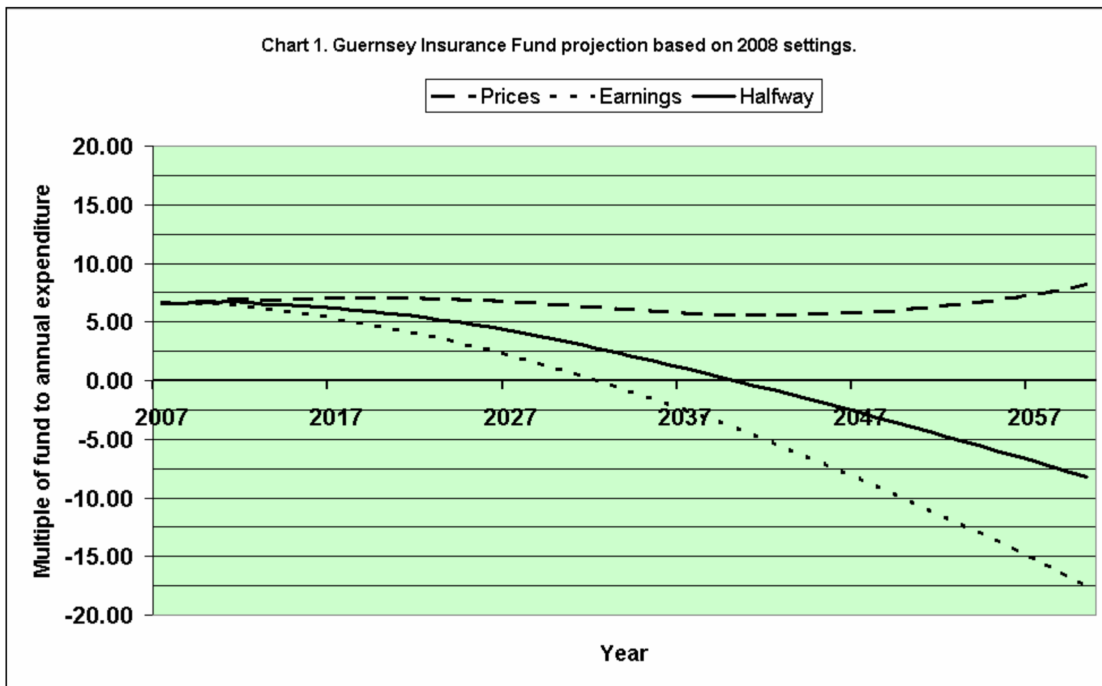
- the external economy
- mortality rates and life-expectancy

106. In order to assist the States in determining the future financing structure for the Guernsey Insurance Fund, the Department has produced a spreadsheet that allows different scenarios to be modelled, as variables are changed. The variables in the model are confined to those that are fully controllable by the States. For the variables that are only partly controllable, or uncontrollable, the model uses a set of central assumptions developed with the assistance of the Government Actuary's Department.

Output of spreadsheet model

107. The spreadsheet displays its results in the form of a chart as shown in Chart 1 below.

108. **It is essential to understand this chart fully, as it is the benchmark against which all of the options and combination of options that follow in the report can be measured and evaluated**.



109. The vertical axis of the chart is a measure of the value of the Guernsey Insurance Fund as a multiple of benefit expenditure and administration costs. For example, in 2008, the chart is based on the Fund having a value of approximately £550m and annual expenditure on benefits and administration is approximately £90m. The cover is therefore approximately 6 times annual expenditure (£550m/£90m).

110. The horizontal axis on the chart is time, from 2008 to 2060.

111. There are 3 lines shown on the chart. The difference between the lines relates to different policies on the uprating of benefits, as follows:

- top line (dashed) increases benefits by prices (RPI) each year
- middle line (solid) increases prices halfway between prices and earnings.
- bottom line (dotted) increases benefits by increase in earnings

112. For the Guernsey Insurance Fund to be sustainable, the relevant line on the chart must not cross the horizontal axis (zero line). To do so would mean that the reserves were fully exhausted and the Fund would be in debt.

113. Chart 1 above shows the projections for the Guernsey Insurance Fund under the following central conditions:

- contribution rates as apply in 2008
- upper earnings limits as in 2008
- upper earning limits increasing in future at half-way point of prices and earnings
- States grant as in 2008 (15% of contribution income)
- pension age of 65
- constant level of total population
- 3% RPI as a long-term average
- economic growth of 2% p.a. in real terms
- 5% p.a. increase in earnings as long-term average (RPI + 2%)
- 200 unemployed as long-term average

114. For simplicity in the financial modelling, the Chart does not separately identify the self-employed and non-employed contributions, but the assumption is that changes in the contribution rates or upper earnings limits for employed persons would also be applied to self-employed and non-employed persons. Changes to the contribution rates or upper earnings limits for employers, would not be applied to the self-employed or non-employed contributions.

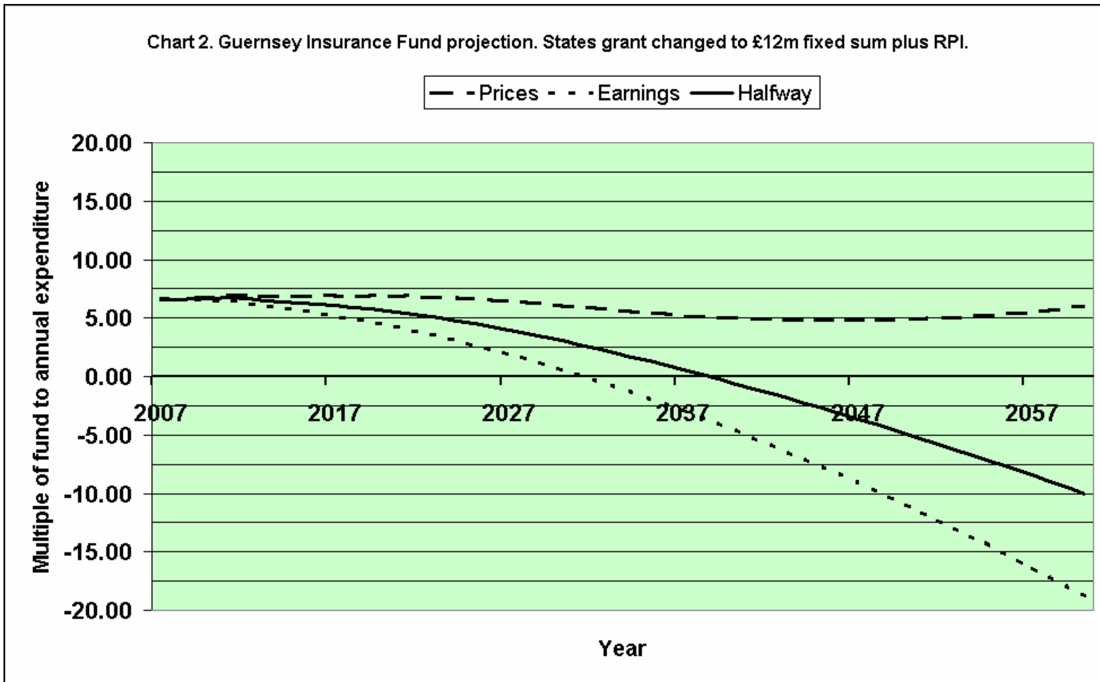
115. It will be noted that, with no alteration of the central assumptions, the Guernsey Insurance Fund is projected to have reduced to zero by 2040. It will also be noted that if future benefit increases were linked only to RPI, the fund does not reduce to zero and the financing of the scheme is sustainable. But for the reasons explained earlier, in paragraphs 69 to 72, the Department would strongly advise against seeing this as a proper solution to the long-term funding issue.

116. The following paragraphs illustrate, though reproducing graphs from the spreadsheet model, the impact on the sustainability of the Fund of changing one or more key variables. **In all cases, the solid line indicating an uprating policy of half-way between prices and earnings is used as the reference point against which to compare the adequacy of various scenarios.**

Changing the States Grant

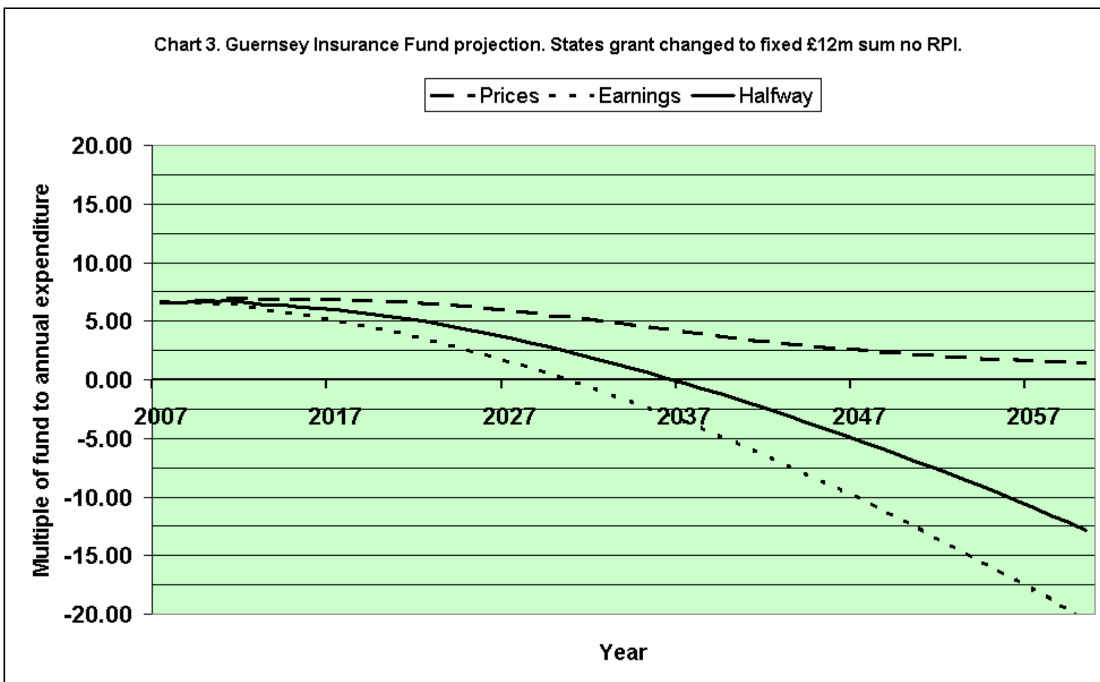
117. If the current formula-led States Grant, equal to 15% of contribution receipts, were changed to a fixed cash sum of £12m, being the approximate 2008 figure,

with annual RPI increases applied, the projected outcome is as shown in Chart 2 below:



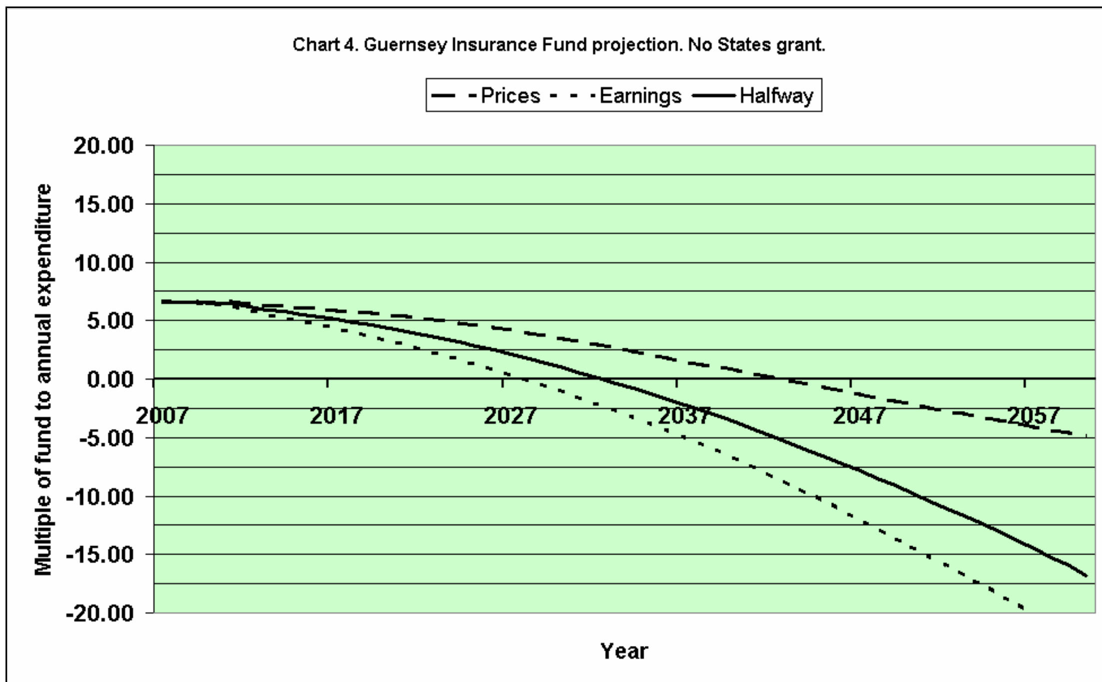
118. While the situation has worsened, with the Fund exhausted by 2038, the effect of changing the indexing of the grant, from contribution receipts to RPI, is seen as relatively minor.

119. Chart 3, below, shows the effect of having a States Grant which is held at £12m per annum, with no increases for RPI.



120. In this scenario, the Fund runs out at 2037, just 1 year earlier than in the previous example. But the rate of decline is a little steeper and hence the corrective measures would need to be more significant.

121. The final example concerning the States Grant shows the effect of having no grant at all, as seen in Chart 4 below:

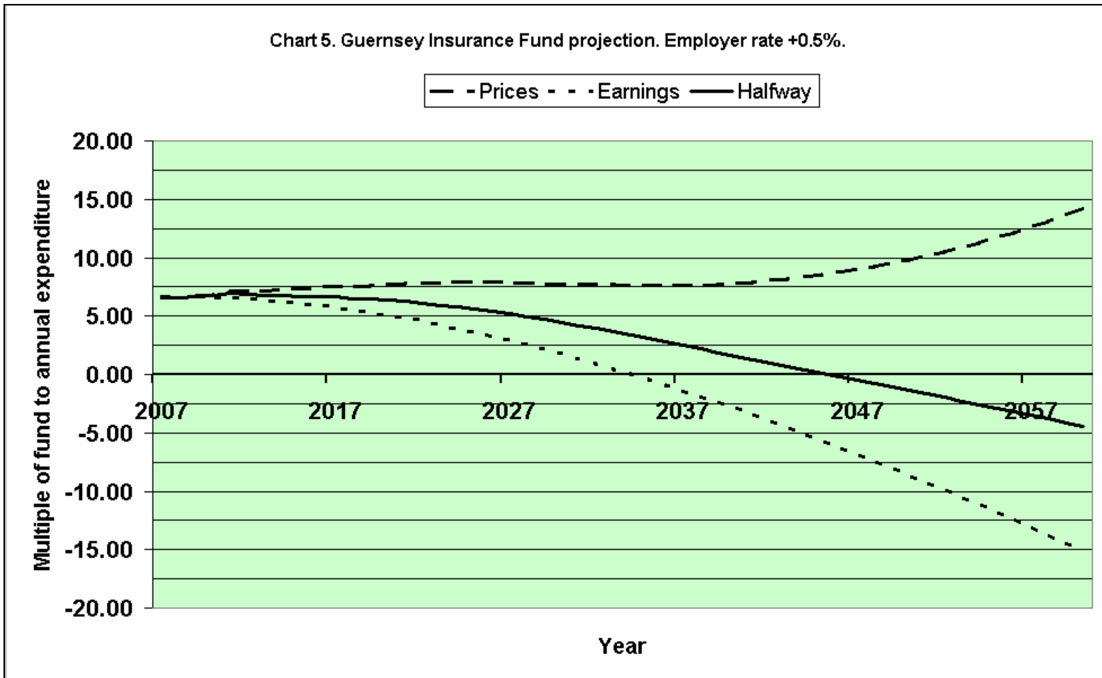


122. In this scenario, the Fund runs out at around 2033. It should be noted that even the RPI benefit uprating line is unsustainable.

123. While, for the mid-point of prices and earnings benefit uprating, all of the foregoing scenarios are unsustainable for the Fund, they serve to show that the States Grant, through its large reductions in the last 2 years, has become a less significant part of the Guernsey Insurance Fund's financing. The solutions for the sustainability of the Fund will not be found solely in that area.

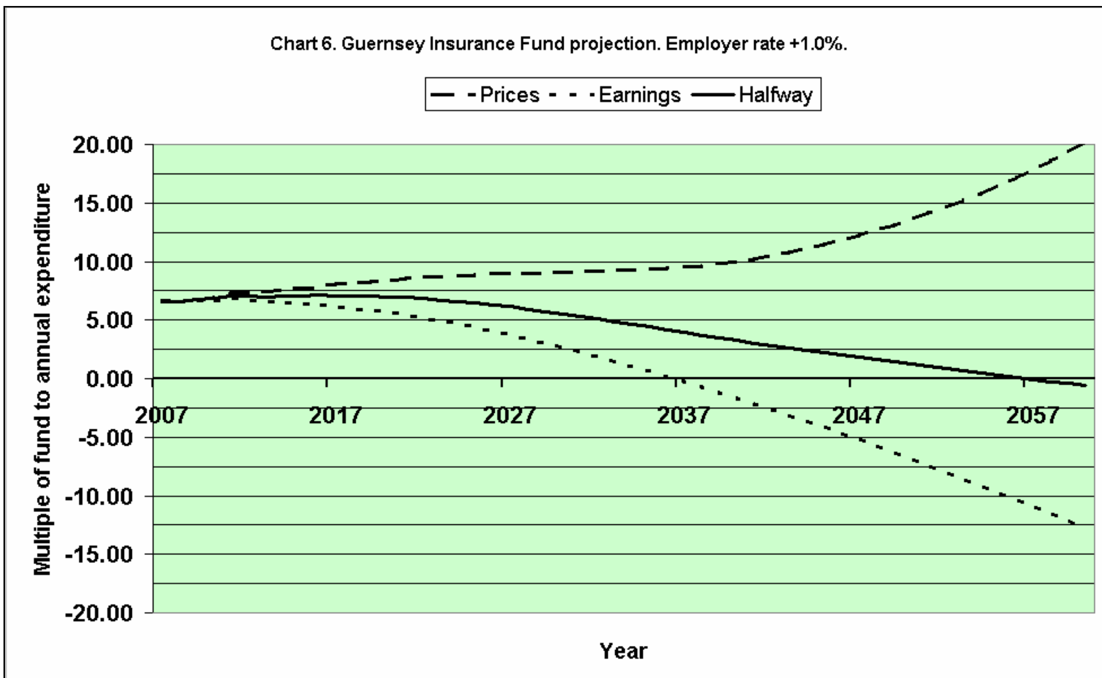
Changing contributions

124. Chart 5, overleaf, takes the States grant back to the current position of 15% of contribution income and shows the effect of increasing the employers' contribution rate by 0.5%, taking the employers' contribution for all three funds from 6.5% to 7.0% of earnings.



125. This has made a more substantial improvement to the central projections under which the Fund was projected to reach zero by 2040. In this scenario, the life of the Fund is extended to 2047.

126. Chart 6, below, shows the effect of further increasing the employers' contribution rate, by a total 1.0%, taking the employers' contribution for all three Funds from 6.5% to 7.5% of earnings.

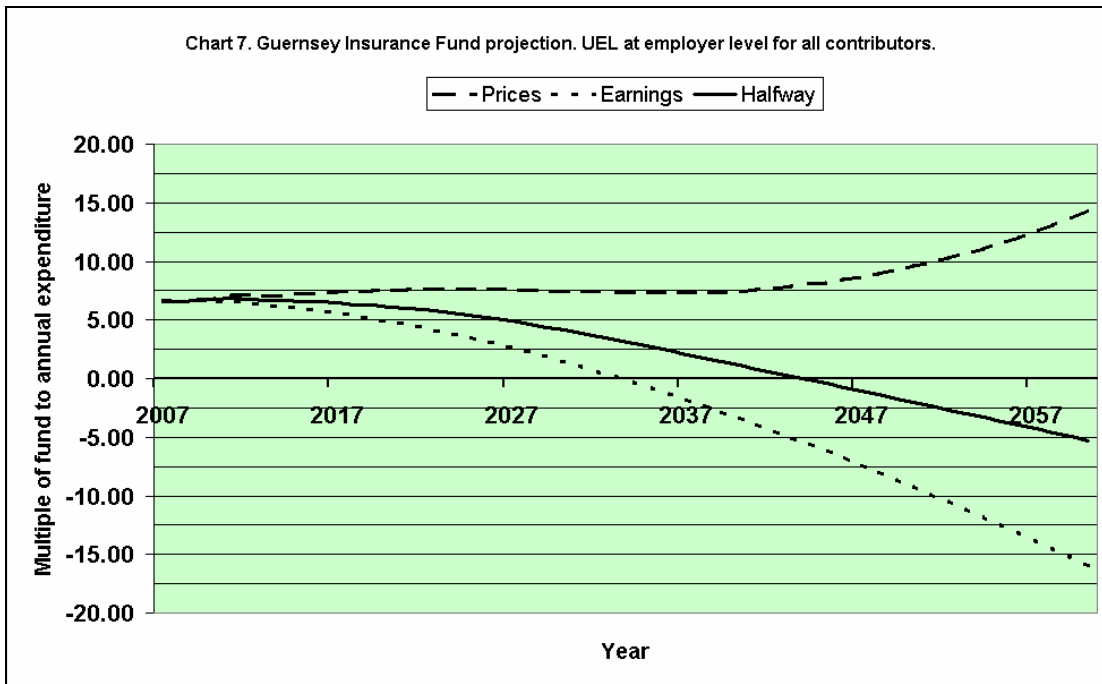


127. This further extends the life of the Fund to 2057.

128. The scenarios involving changed contribution rates show that this is the main opportunity for ensuring sustainability of the Fund.

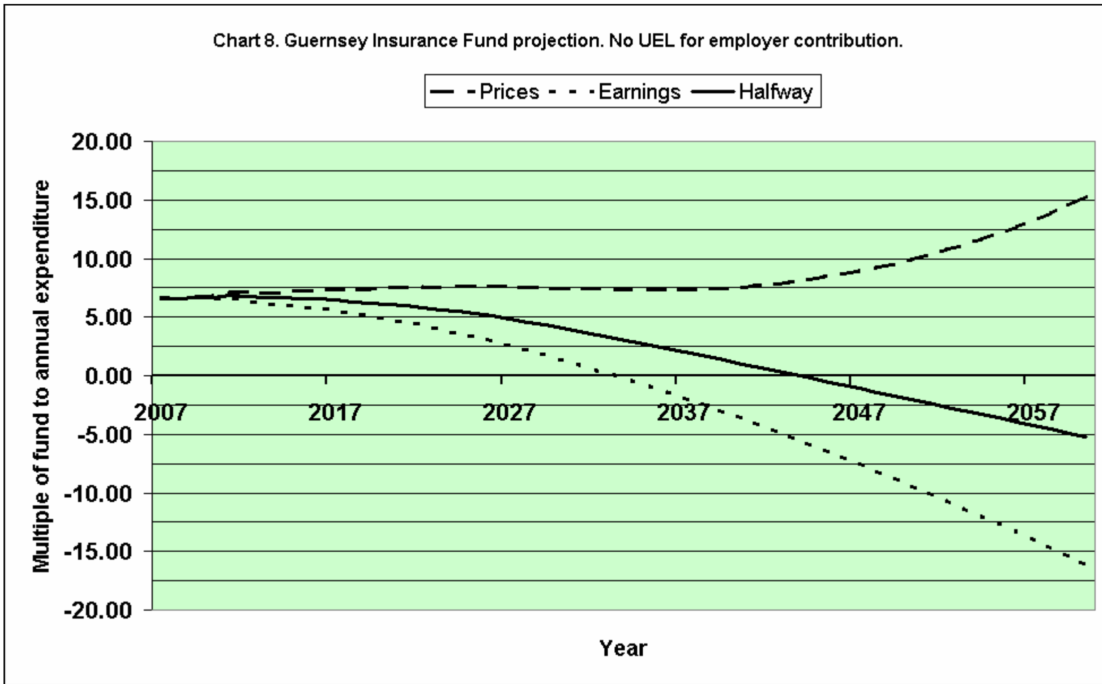
Changing the upper earnings limits

129. Chart 7, below, shows the effect of increasing the upper earnings limit for all contributors to the same, higher, level that currently applies to employers. In 2008 terms, this would mean increasing the annual upper earnings limit for all contributors from £64,896 to £108,108.



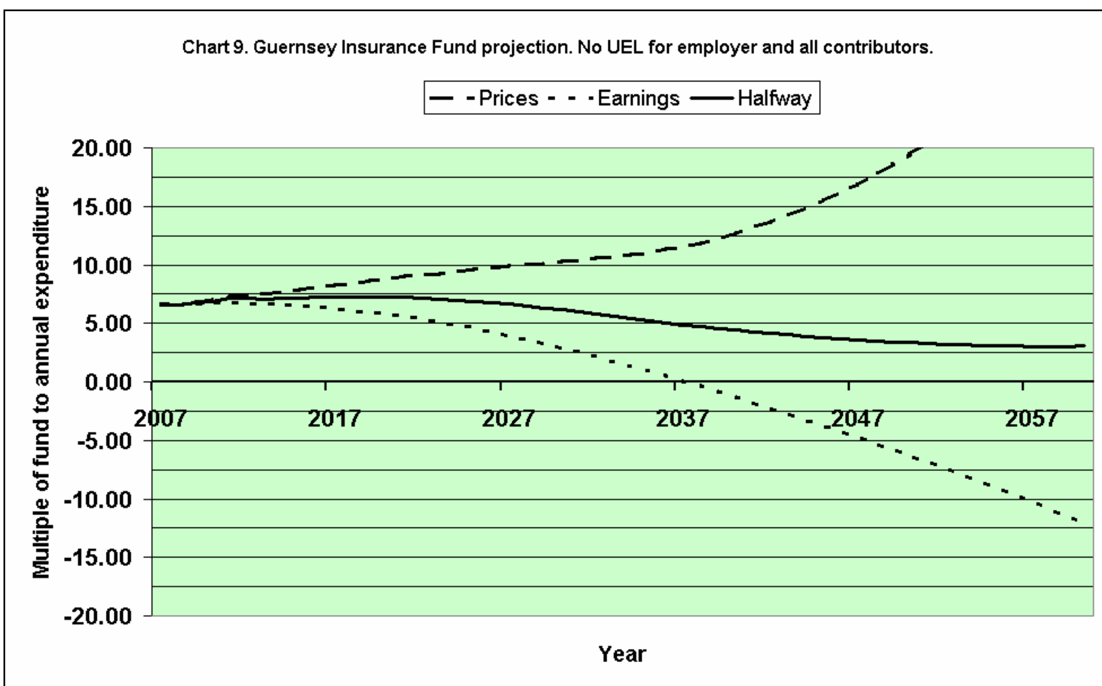
130. Under this scenario, the Fund runs out in 2044.

131. Chart 8, overleaf, shows the effect of removing the upper earnings limit entirely for the employers' contribution.



132. Under this scenario, the Fund runs out in 2044.

133. The final chart on upper earnings limits, Chart 9, shows the effect of removing the upper earnings limit entirely for all contributors, as well as for the employers.

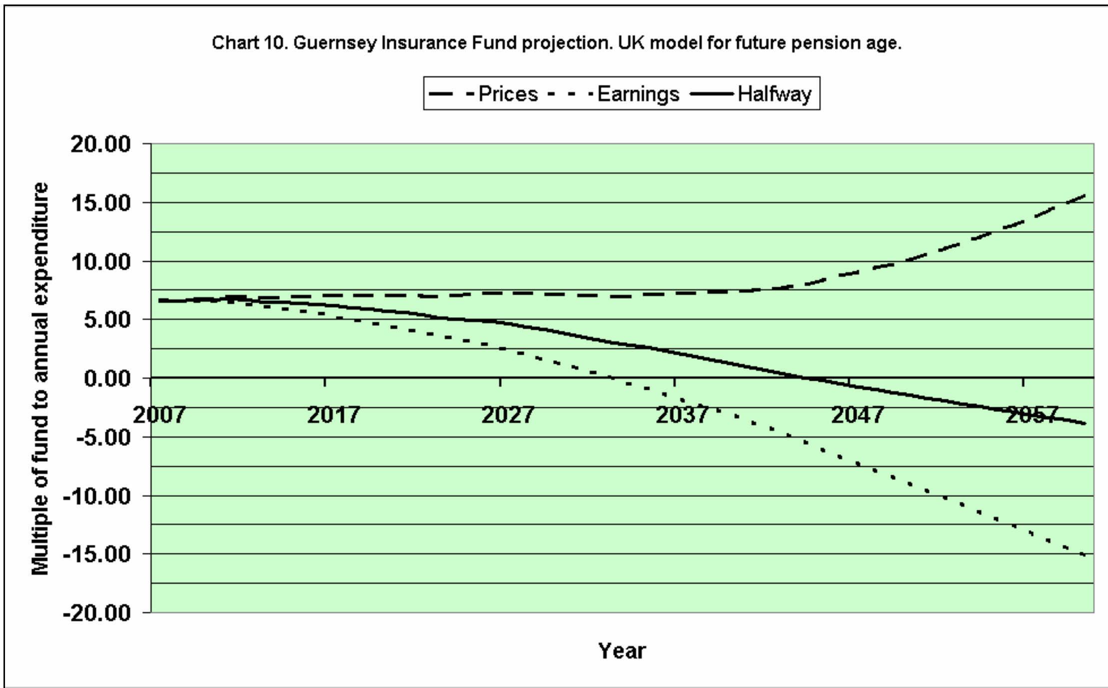


134. Under this scenario, the Fund does not run out, but continues at a multiple of approximately 2.5 times annual expenditure at the end of the projection period in 2060. This chart is the first sustainable view that has been shown in this report.

However, this particular scenario assumes that unlimited contribution liabilities can be secured from the very highest earning employed, self-employed and non-employed residents in the community. The model has not factored in any offsets in respect of behavioural changes such as moving very highly paid employees to other jurisdictions or other avoidance measures.

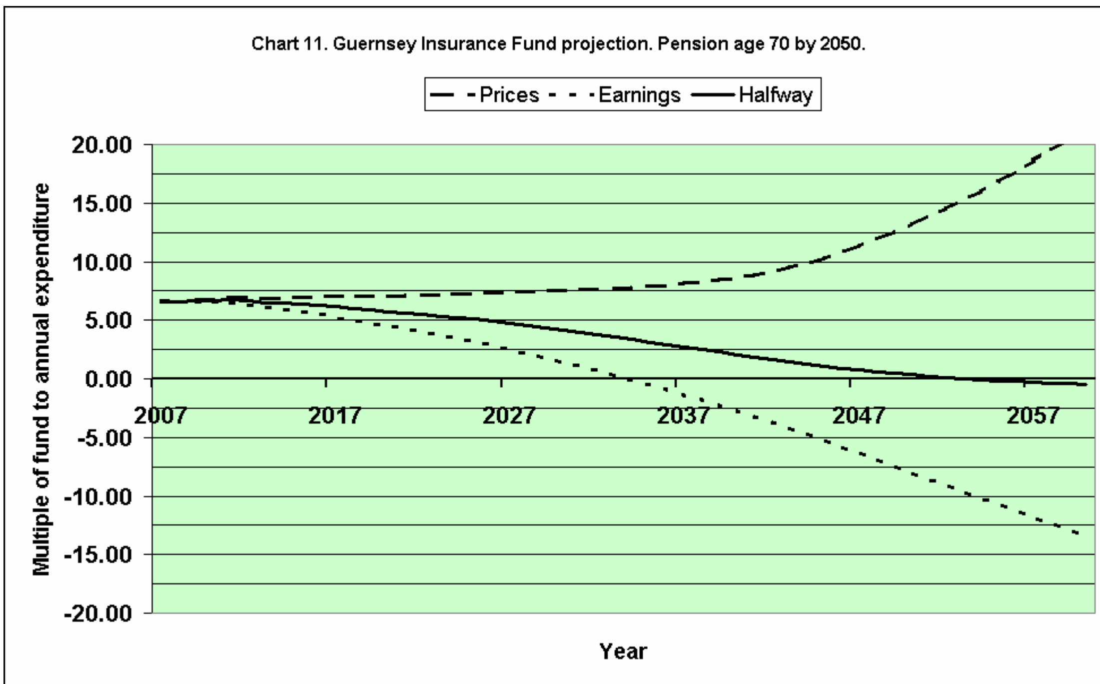
Changing pension age

135. Chart 10, below, shows the effect of increasing the pension age from 65 to 68 between 2024 and 2046 to mirror the changes approved in the UK.



136. Under this scenario, the Fund runs out in 2045. The marginal improvement reflects the long time period over which the increased pension age will be given effect.

137. Chart 11, overleaf, shows the effect of increasing the pension age from 65 to 70 between 2020 and 2050, as put forward in this report (paras. 82 to 89) as an option for Guernsey.



138. Under this scenario, the Fund runs out in 2053, but is very close to sustainability. The improvement in the position compared with that for the UK pension age reflects the fact that pension age would be increasing at a faster rate than in the UK and reaching a higher ultimate position.

Changing more than one variable at a time

139. All of the charts shown up to this point in the report have taken the central assumptions and changed only on of the several variables. This has been useful in order to gauge the relative impact of each variable. The exercise has shown that the States Grant is less significant than it has been historically. Contribution rates, upper earnings limits and pension age remain highly significant.

140. The answer to ensuring the sustainability of the contributory social security schemes will almost certainly, in practice, involve changing two or more of the variables at the same time. This gives rise to a number of scenarios which is too large to show as charts in this report.

141. The preferred scenario of an individual member of the community will perhaps be a matter of taste and will be shaped by what is the most important factor to that person. For example, if the most important thing is for pension age to remain at 65, then the solution will involve increasing the contribution rates for contributors, or employers or increasing upper earnings limits, or some combination of those things.

142. If the most important thing is for there to be no increase in contribution rates for individual contributors, then the solution will involve increasing the employers'

contribution rate, perhaps combined with increasing upper earnings limits or increasing pension age.

Some sustainable scenarios

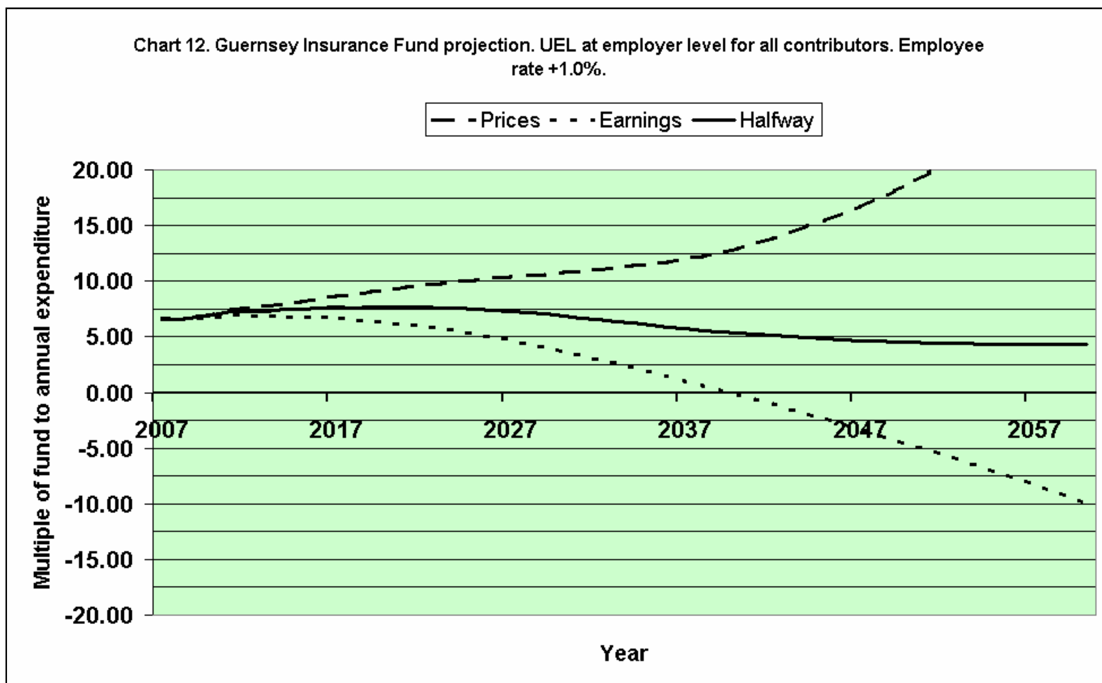
143. The final seven charts all involve changing more than a single variable in order to produce a sustainable outcome for the Guernsey Insurance Fund. The scenarios are just 4 of many and are not ranked in any order of preference by the Department.

Keeping pension age at 65

144. If keeping pension age at 65 is the main issue, a sustainable outcome could be found by:

- Maintaining States grant at 15% of contribution income
- Increasing employee upper earnings limit to match employer
- Increasing employers' contribution rate by 1%

as seen in Chart 12 below.

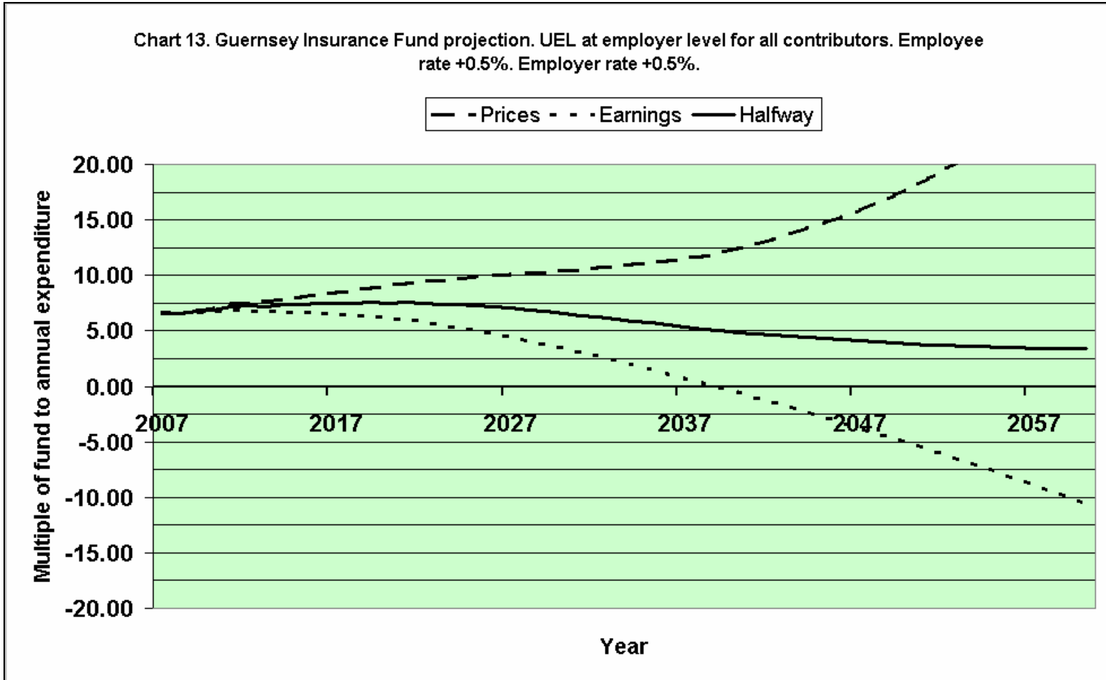


145. A variation to Chart 12 would be to share the extra contribution burden between the employer and the employee, by applying the following criteria:

- Maintaining States grant at 15% of contribution income
- Increasing employee upper earnings limit to match employer
- Increasing employers' contribution rate by 0.5%

- Increasing employees' contribution rate by 0.5%

as seen in Chart 13 below.



146. A further variation would be to maintain the current upper earnings limits and to increase the rate of contribution for the employer and the employee, as follows:

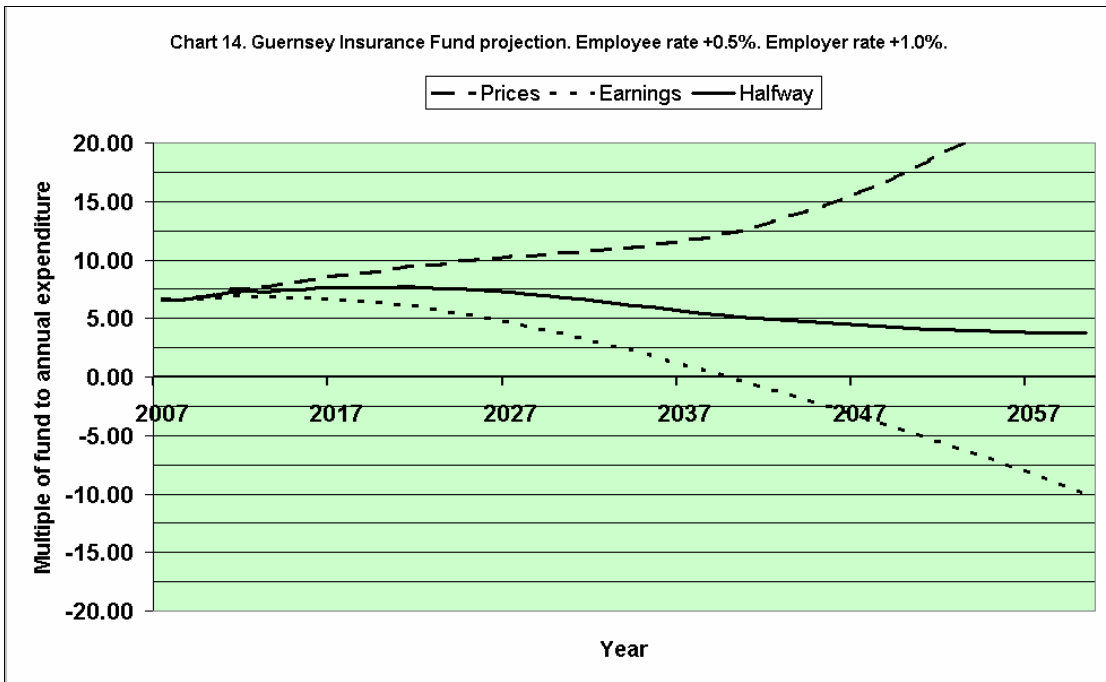
- Maintaining States grant at 15% of contribution income

- Maintaining current upper earnings limits

- Increasing employers' contribution rate by 1.0%

- Increasing employees' contribution rate by 0.5%

as seen in Chart 14 overleaf.

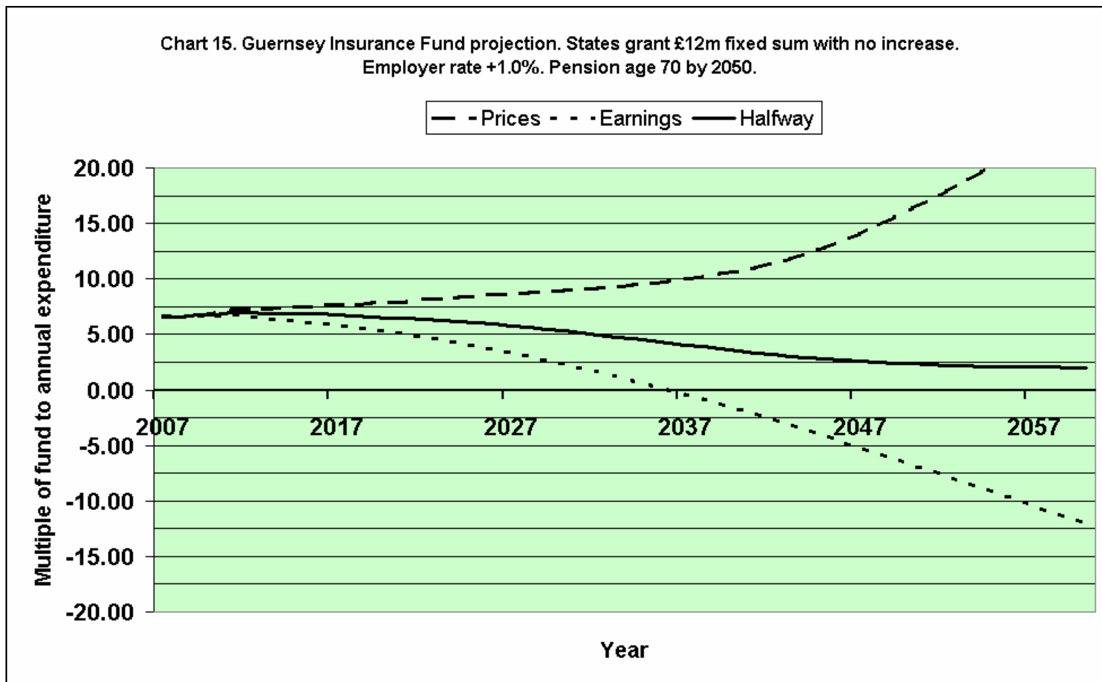


Limiting the expenditure on the States Grant

147. If limiting the expenditure on the States grant was the main issue, a sustainable outcome could be found by:

- Maintaining States grant at £12m with no annual increases
- Increasing employers' contribution rate by 1%
- Increasing employers' contribution rate by 1%
- Increasing pension age from 65 to 70 between 2020 and 2050

as seen in Chart 15 overleaf.

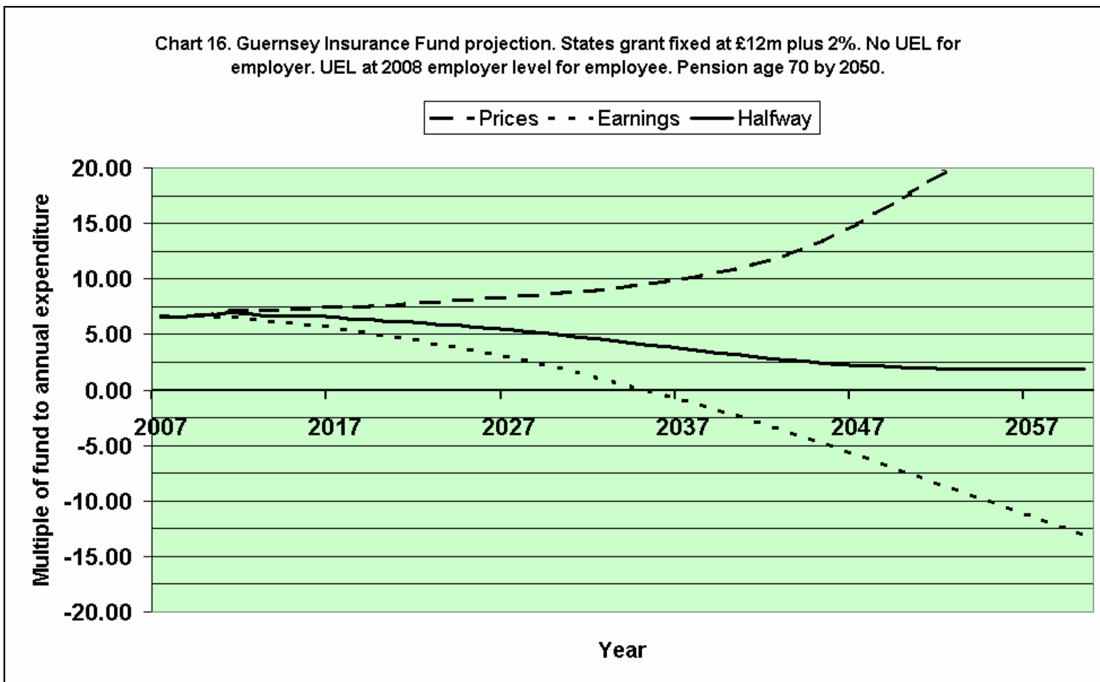


Maintaining contribution rates and limiting the States Grant

148. If keeping contribution rates at current levels, while limiting expenditure on the States Grant were the main issues, a sustainable outcome could be found by:

- Removing upper earnings limit on employers' contributions
- Increasing employees' upper earnings limit to current level for employers (£108,108 p.a)
- Maintaining States grant at £12m with 2% annual increases
- Increasing pension age from 65 to 70 between 2020 and 2050

as seen in Chart 16 overleaf.

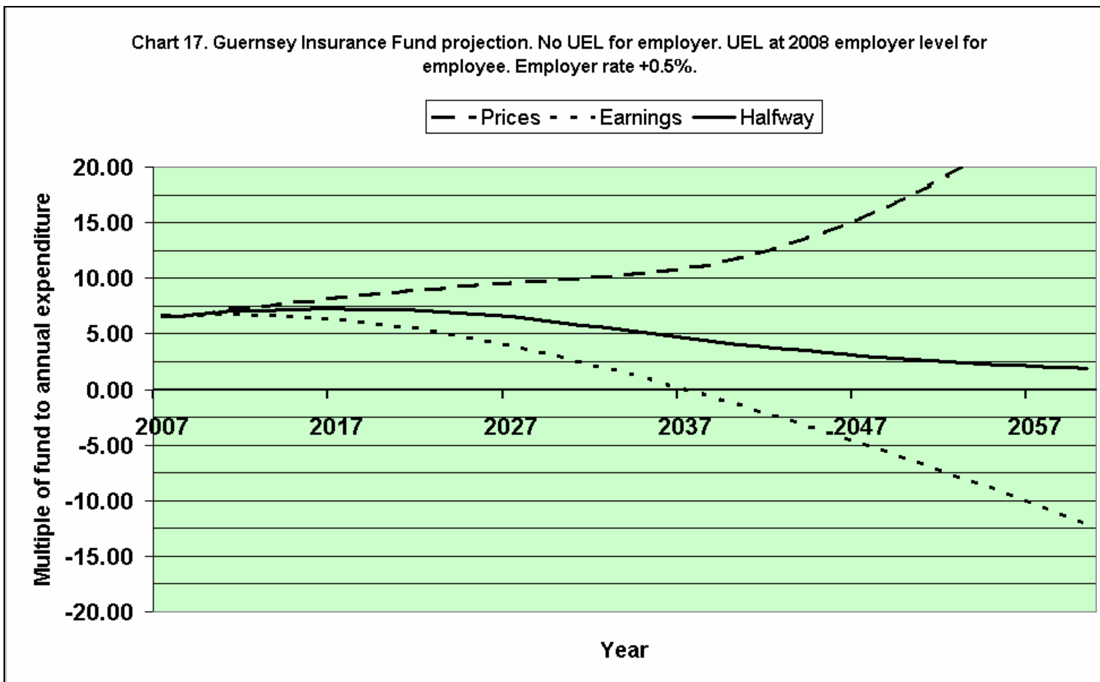


Minimising increase in contribution rates and no increase in pension age

149. If limiting the increases in contribution rates, while maintaining pension age at 65 were the main issues, a sustainable outcome could be found by:

- Continuing with States grant of 15% of contribution income
- Maintaining pension age of 65
- Removing upper earnings limit on employers' contributions
- Increasing employees' upper earnings limit to current level for employers (£108,108 p.a)
- Increasing employers' contribution rate by 0.5%

as seen in Chart 17 overleaf.

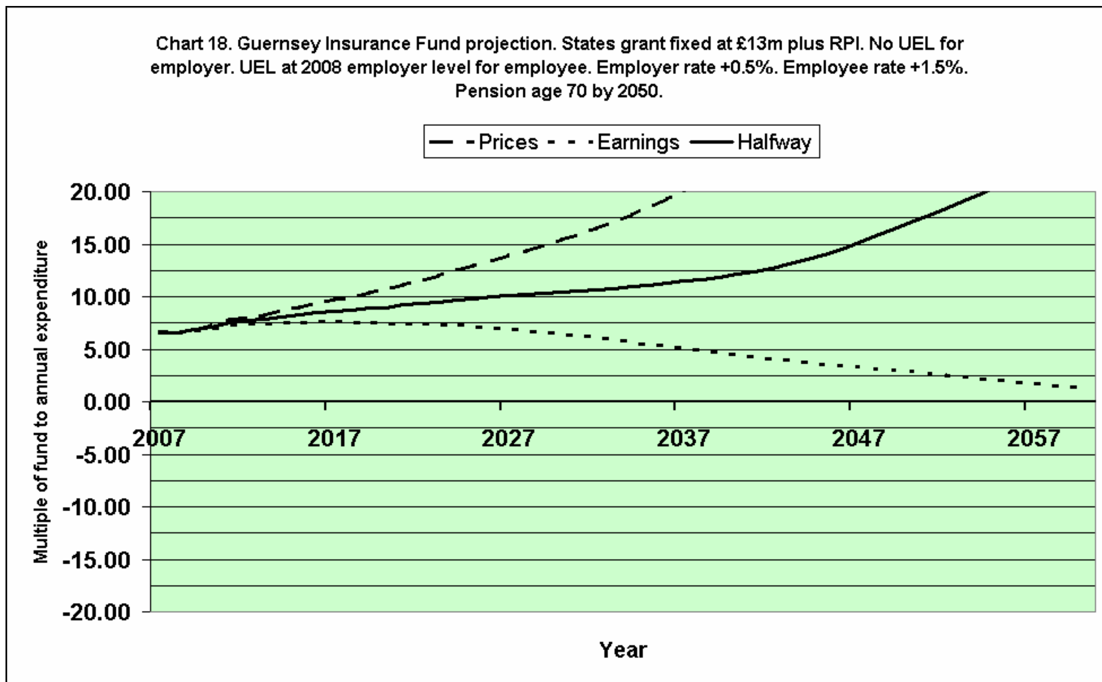


Uprating pensions by earnings

150. If it were decided that pensions should be increase annually in line with the increase in earnings instead of the customary mid-point between prices and earnings, a sustainable outcome could be found by:

- States grant of £13m plus RPI annual increases
- Removing upper earnings limit on employers' contributions
- Increasing employees' upper earnings limit to current level for employers (£108,108 p.a)
- Increasing employers' contribution rate by 0.5%
- Increasing employees' contribution rate by 1.5%. (Employees would be the beneficiaries of the better level of pensions)
- Increasing pension age from 65 to 70 between 2020 and 2050

as seen in Chart 18 overleaf.



Conclusion

151. Guernsey's contributory social security schemes are at present in a strong financial position and continue to provide a range of social protection benefits which are essential to the financial wellbeing of many residents.

152. Looking to the future, the schemes will face the financial pressures of the demographic changes, in particular the substantial growth in the number of people in retirement compared with the number at work. The schemes also need to have resolved the future of the States grants from general revenue and the consequences of further reducing those grants as part of Guernsey's economic and taxation strategy.

153. But these are problems to which there are some readily found solutions. The challenge for the States is to identify the most appropriate of those solutions or, more likely, combination of solutions.

154. This report is intended as a consultation document and is not a report that requires firm positions to be taken. But it will be most helpful to the Social Security Department, in preparing a subsequent report to the States in 2009, to have an indication of how the States would respond to the following questions:

1. Should the States grants from General Revenue to the Guernsey Insurance Fund and Guernsey Health Service Fund continue in their current form, being 15% of contribution income and 12% of contribution income respectively?

2. Should the States grants instead be linked to RPI, or some variation of RPI or frozen at their current level?

3. Should the upper earnings limits for employees, employers, self-employed and non-employed be increased to ensure the sustainability of the funds?

4. Should contribution rates for employees, employers, self-employed and non-employed be increased to ensure the sustainability of the funds?

5. Who should bear the burden of any higher contribution rates, individual contributors or employers, or both?

6. Should pension age remain at 65 or should it increase over time?

155. The Department is hopeful that this report contains sufficient material to give rise to an informed debate on these issues and looks forward to hearing the opinions of members of the States and, importantly, the views of the residents of Guernsey and Alderney to whom this consultation is being extended.

Recommendation

156. The Department is keen for debate on this report to address the general policy issues contained without taking a definitive position on any of those issues. The Department wishes to have the opportunity to reflect on all feedback from the consultation exercise and to consult further with the Treasury and Resources Department before returning to the States with detailed proposals. The Department, therefore, requests that the recommendation which follows be considered by the States without amendment in accordance with Rule 12(4) of the Rules of Procedure of the States of Deliberation.

157. The Department recommends:

> That the Social Security Department, having regard to issues raised in the consultation process, report to the States during 2009 with proposals to ensure the financial sustainability of the contributory social security schemes.

Yours faithfully

M H Dorey
Minister

(NB The Policy Council has no comment on the proposals.)

(NB The Treasury and Resources Department has no comment on the proposals.)

The States are asked to decide:-

Whether, after consideration of the Report dated 26th September, 2008, of the Social Security Department, they are of the opinion:-

That the Social Security Department, having regard to issues raised in the consultation process, report to the States during 2009 with proposals to ensure the financial sustainability of the contributory social security schemes.

(NB The Social Security Department has requested that this matter be debated in accordance with Rule 12 (4) of the Rules of Procedure of the States of Deliberation which provides

"Where a Department or Committee originating a matter for debate before the States is of the opinion that the proposals it is submitting to the States are ones of general policy, and where it is desirable that the general principles of that policy should be considered, the Department or Committee may request that its propositions be considered by the States without amendment, on the understanding that if the propositions are accepted, the Department or Committee would return with detailed proposals which could be accepted or rejected, together with any amendments…")

IN THE STATES OF THE ISLAND OF GUERNSEY ON THE 10th DAY OF DECEMBER, 2008

The States resolved as follows concerning Billet d'État No XVII dated 14th November 2008

SOCIAL SECURITY DEPARTMENT

FINANCING OF CONTRIBUTORY SOCIAL SECURITY SCHEMES

After consideration of the Report dated 26th September, 2008, of the Social Security Department:-

That the Social Security Department, having regard to issues raised in the consultation process, report to the States during 2009 with proposals to ensure the financial sustainability of the contributory social security schemes.

K H TOUGH
HER MAJESTY'S GREFFIER