Pensions

When medical students, we were discussing the advantages of taking a year to do an intercalated BSc. One of our number pointed out that it would reduce by one year the career earnings towards a pension! None of the rest of us had ever thought about pensions, but it is a topic which gains in importance throughout working life.

To understand pension policy, the arrangements have to be looked at from several viewpoints, actuarial, economic, social and demographic. A modern state has a need to ensure that those who can no longer work have financial provision for their old age. The more adequate the pensions, the less the State will have to pay out in welfare benefits. Pension funds are an important component of national investment. Pensions legislation allows earnings to be withheld, and invested to provide for retirement. Either the employee can contribute real money, or enjoys a non-contributory pension while being paid a lower salary. The Armed Forces Pension Scheme is non-contributory and the Pay Review Bodies publish the notional deductions which ‘fund’ the pension. A consequence of the Social Security Act (1986) is that gratuity paying Short Service Commissions are contrary to the spirit of the law. It is almost certain that gratuities will be replaced by either a deferred pension, or transferrable pension rights. While we may regret the loss of the gratuity, on broader social grounds we must agree that it is right for the State to insist that all employers make provision for the retirement of their employees.

Other provisions both allow individuals to opt out of contributory schemes and permit existing occupational schemes to be topped up by means of Additional Voluntary Contributions (AVC). These may be either in-house, or free standing schemes offered by commercial companies. Everyone will now have the opportunity to invest in a pension up to the limits set by the Inland Revenue.

Pensions legislation has been a traditional battleground between the Inland Revenue and social and economic interests. Pension schemes are a postponement of income, a transfer of money from a high earning, high tax paying working life, to a lower income, lower taxpaying retirement. The tax privileges of pension schemes have to be limited by Inland Revenue rules, because otherwise they could be abused by tax avoidance devices. Before this year, the Inland Revenue would not allow those with an occupational pension to take out additional policies. The government has now relaxed this restriction, clearly recognising that the long term economic and social benefits of pension schemes outweigh short term loss of tax revenue. Nevertheless restrictions remain, the most important being that final pension cannot exceed two thirds of salary, and that the maximum percentage of income which can be invested in a pension is limited. As with all other tax regulations there is a need to read the small print.

The Armed Forces Pension Scheme has often been criticised, but in commercial terms it is a good proposition. As might be expected, it is biased towards youth and early retirement. To earn a pension after sixteen years would cost a high price in a commercial scheme. The MOD justifies this by the Service requirement to employ young people. It is less advantageous in later life and positively disadvantageous after thirty-four years service. Because an annuity is worth less at a later age, any officer serving beyond thirty-four years is losing from his notional pension capital. The Armed Forces Pension Scheme provides retired pay according to rank, and this disadvantages those who earn significant additional pay. These include doctors, dentists, aircrew and submariners. For some years a debate has run within the MOD arguing the case for pay related, rather than rank related pension. However, pensions have to be funded and any increase of pension will require a reduction in the additional pay. The new legislation has solved the question, because servicemen can now buy an additional pension.

The National Health Service Superannuation Scheme is typical of public sector schemes. A fraction of basic salary is earned for each year of service. Those who have made the detailed calculations necessary to compare the two schemes, will have discovered that for comparable professional careers, the Armed Services Scheme is advantageous up to about the age of 60, and disadvantageous thereafter. It is government policy to encourage job and pension mobility, so people should be able to transfer between public sector schemes. It is important to note that transfer will be calculated on the accumulated value, and not on a simple counting of years of service.

Although the Social Security Act (1986) allows individuals to opt out of occupational schemes, no one in their senses would leave a non-contributory pension scheme, because they are paying through a reduced salary. The effect of the legislation on service personnel will be twofold. Those on short service engagements can expect to earn a deferred pension and not a gratuity.

Secondly all career personnel now have the opportunity to increase their pension through Additional Voluntary Contributions. For doctors and dentists on full careers, their rank related pension will be less than half of final salary. The limit of contribution is 15% of salary from which must be deducted any contributions which some are paying to improve their widows pension or to purchase additional years. For the younger
personnel, it is their final salary which will limit their investment; for the more senior it will be the percentage of income which will prove the limiting factor.

This new legislation means that all should now review their pension prospects. The income tax concessions on pension schemes make them unmatchable investments. The flexibility of commercial schemes allows you to tailor the investment to your mood. Alternatively you can wait until the MOD announces their in-house AVC scheme this year. For the late entrant the existing option of buying additional years remains a third alternative.

As for other investments, the advice must be to consult a good broker. Pensions law is complex, individual needs vary, and general information is no substitute for individual professional advice. Pensions are long term contracts and errors are expensive to correct.

**HONORARY CONSULTANTS TO THE ARMY**

Dr P J F Baskett, FFARCS, has been appointed Honorary Consultant in Resuscitation to the Army with effect from 1 February 1988.

Dr Ian D C Douglas, FRCPPath, has been appointed Honorary Consultant in Haematology to the Cambridge Military Hospital with effect from 4 November 1987.

Professor A P Adams, MA, MB, FFARCS, has been appointed Honorary Consultant in Anaesthetics to the Army with effect from 1 February 1988.